

# ARTICLES

## Reforming Legal Ethics in a Regulated Environment: An Introductory Overview

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### INTRODUCTION: THE FBA AND ALI-ABA CONFERENCE ON LAWYER AND ACCOUNTANT LIABILITY AND RESPONSIBILITY

Among the aftershocks of the Savings and Loan (S&L) debacle were a series of large and highly visible settlements between the government and some of the nation's leading law and accounting firms and their individual partners and associates. Settlement figures ran into the hundreds of millions of dollars. Perhaps the most well-known case was that involving the prominent New York law firm of Kaye, Scholer, Fierman, Hays & Handler and three of its partners. On March 2, 1992, the Office of Thrift Supervision (OTS) issued administrative charges against them, claiming payment of restitution in the sum of \$275 million for alleged losses suffered as a result of the firm's representation of a California thrift, Lincoln Savings & Loan Association.<sup>1</sup> The OTS simultaneously imposed an asset freeze order on the firm, the first such order ever imposed by a banking agency against *any* law firm.<sup>2</sup> The firm and its partners settled the claim within a week, agreeing, among other things, to pay \$41 million to the thrift's receiver without admitting or denying liability. While less drastic (but still severe) enforcement action had already been taken by the OTS against other law firms and

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1. *In re* Fishbein, Katzman, Fisher & Kaye, Scholer, Fierman, Hays & Handler, OTS AP-92-19 (1992) (Notice of Charges and of Hearing for Cease and Desist Orders to Direct Restitution and Other Appropriate Relief) [hereinafter *Kaye, Scholer*]. In addition to the claim for monetary relief, the OTS charges sought various injunctive relief against both the firm and three of its partners.

2. See *In re* Fishbein et al., [1992-1993 Transfer Binder] Federal Banking L. Rep. (CCH) ¶89,040 (Mar. 1, 1992) (issuing a temporary order to cease and desist).

lawyers,<sup>3</sup> the Kaye Scholer action served more than any other event to catch the attention of the legal profession and the public through national coverage and front-page publicity.

*L'Affaire Kaye Scholer*, and subsequent proceedings by federal banking agencies<sup>4</sup> against lawyers and law firms, generated intense professional and public debate regarding the fairness of the governmental action and the integrity and reputation of the lawyers involved. Some of the government's central claims against the lawyers involved were based, not merely on orthodox allegations of misfeasance, but upon assertions and interpretations of legal and ethical standards regarded by many lawyers as novel and unprecedented. The application of these standards raised instant controversy. The Business Law Section of the American Bar Association (ABA) had appointed a task force to consider the implications of the government claims against lawyers prior to the *Kaye Scholer* case.<sup>5</sup> However, immediately following the *Kaye Scholer* settlement, the ABA President independently appointed a large-scale Working Group on Lawyers' Representation of Regulated Clients (Working Group) to review and analyze the legal and ethical issues arising out of the cases.<sup>6</sup> The New York City and County Bar Associations condemned the OTS actions in *Kaye Scholer*, recommending statutory amendments to the regulators' enforcement powers,<sup>7</sup> and the City

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3. See *In re Jacobs and Sherman & Howard*, OTS AP-91-33, AP-91-34, AP-91-35, AP-91-36 (1991) (detailing Ronald H. Jacobs & the law firm of Sherman & Howard's settlement offer which limited the parties' scope of representation on behalf of federally insured depository institutions); *In re Stroud*, OTS AP 91-30 (1991) (revoking attorneys' privilege to practice before the OTS); *In re Ingram*, OTS AP 91-28 (1991).

4. The OTS, which supervises savings associations (thrifts), is only one of the agencies involved. A number of federal government agencies exercise supervisory and enforcement responsibility over federally insured depository institutions (commercial banks, thrifts, and credit unions) and their "institution-affiliated parties" (including lawyers and accountants). These agencies include the Board of Governors of the Federal Reserve System (bank holding companies, foreign banks, and state member banks), the Office of the Comptroller of the Currency (national banks and federally licensed foreign bank offices), the Federal Deposit Insurance Corporation (FDIC) (state nonmember banks and, as backup enforcer, all federally insured banks and thrifts), and the National Credit Union Administration (federally insured credit unions). The OTS is the only agency among these that has taken significant enforcement action against lawyers and law firms, but the FDIC and another federal agency, the Resolution Trust Corporation (RTC), in their capacities as receivers for failed banks (the FDIC) and thrifts (the RTC), have been plaintiffs in a large number of malpractice lawsuits against lawyers, law firms, and accounting firms.

5. See Keith R. Fisher, *Statutory Construction and the Kaye Scholer Freeze Order*, reprinted in REFORMING LEGAL ETHICS IN A REGULATED ENVIRONMENT 371 (1994) (publishing an exposure draft). Mr. Fisher was the chair of the Task Force on the Liability of Counsel Representing Depository Institutions.

6. See LABORERS IN DIFFERENT VINEYARDS?: THE BANKING REGULATORS AND THE LEGAL PROFESSION v-vii, xv-xix (Jan. 1993), reprinted in part in REFORMING LEGAL ETHICS IN A REGULATED ENVIRONMENT 235 (1994) (detailing the composition and proceedings of the Working Group) [hereinafter LABORERS IN DIFFERENT VINEYARDS?].

7. See N.Y. State Bar Ass'n Resolution, adopted April 4, 1992 (recommending that 12 U.S.C. § 1818(c)(1) be amended to allow the imposition of freeze orders by regulatory agencies only after

Bar Association's Committee on Professional Responsibility produced a report on the discipline of law firms.<sup>8</sup> Professional journals and newspapers ran one story after another as each new case was settled. Few other subjects have occupied as much space in the recent academic law reviews and curricula of continuing legal education programs as has the question of lawyer liability in regulatory practice.<sup>9</sup>

The ABA itself, accepting the recommendations of the Working Group,<sup>10</sup> adopted resolutions: (1) calling on Congress to reform the law upon which the enforcement actions had been based; (2) calling on the banking agencies to moderate their use of enforcement powers when interacting with lawyers representing insured depository institutions and to employ proper rulemaking proceedings when adopting novel interpretations of applicable codes of professional responsibility; and (3) referring a number of disputed interpretations of the *Model Rules of Professional Conduct* (*Model Rules*) to the ABA Standing Committee on Ethics and Professional Responsibility for formal opinions.<sup>11</sup>

While all this was going on, the principal regulatory lawyers involved were active — making speeches and distributing memoranda aimed at articulat-

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the provision of notice and upon a showing that the agency is likely to succeed on the merits); see also Comm. on Professional Responsibility of the Ass'n of the Bar of the City of N.Y., *Attachment of Law Firm Assets by Federal Regulatory Agencies* (Mar. 1992), reprinted in REFORMING LEGAL ETHICS IN A REGULATED ENVIRONMENT 265, 272 (1994) (recommending the amendment of 12 U.S.C. § 1818 to provide for judicial approval before a temporary freeze order can be imposed).

8. Comm. on Professional Responsibility of the Bar of the City of N.Y., *Discipline of Law Firms* (May 1993), reprinted in REFORMING LEGAL ETHICS IN A REGULATED ENVIRONMENT 249 (1994) [hereinafter *Discipline of Law Firms*].

9. The list of publications is too lengthy to reproduce here. The following, in addition to works cited elsewhere in this Article, are some of the more substantial works, both sympathetic and hostile to the government's action, that have ethical issues as their principal focus: *In the Matter of Kaye, Scholer, Fierman, Hays & Handler: A Symposium on Government Regulation, Lawyers' Ethics, and the Rule of Law*, 66 S. CAL. L. REV. 977-1220 (1993); *Symposium: Lawyer and Law Firm Liability to Regulators and Shareholders*, 12 REV. LITIG. 513-663 (1993); Robert G. Day, *Administrative Watchdogs or Zealous Advocates? Implications for Legal Ethics in the Face of Expanded Attorney Liability*, 45 STAN. L. REV. 645 (1993); Joyce A. Hughes, *Law Firm Kaye, Scholer, Lincoln S&L and the OTS*, 7 NOTRE DAME J.L. ETHICS & PUB. POL'Y 177 (1993); Peter C. Kostant, *When Zeal Boils Over: Disclosure Obligations and the Duty of Candor of Legal Counsel in Regulatory Proceedings after the Kaye Scholer Settlement*, 25 ARIZ. ST. L.J. 487 (1993).

10. The recommendations were accompanied by a final report and updating appendix of the Working Group and were supported by the ABA standing committees on Ethics and Professional Responsibility and Lawyers' Professional Liability, and the ABA sections of Administrative Law and Regulatory Practice, Antitrust Law, Litigation, Real Property, Probate and Trust Law. WORKING GROUP ON LAWYERS' REPRESENTATION OF REGULATED CLIENTS, AM. BAR ASS'N, REPORT TO THE HOUSE OF DELEGATES (June 1993), reprinted in REFORMING LEGAL ETHICS IN A REGULATED ENVIRONMENT 217 (1994) [hereinafter FINAL REPORT]. The recommendations were adopted unanimously by the ABA House of Delegates in August 1993.

11. Anticipating the recommendations of the Working Group, the standing committee had already responded with its first opinion. ABA Comm. on Ethics and Professional Responsibility, Formal Op. 93-375 (1993).

ing more clearly their expectations of lawyers<sup>12</sup> and, in the case of the OTS, preparing a response to the Working Group's views.<sup>13</sup> In the judicial arena, one of the most important civil suits addressing the responsibilities of lawyers and law firms in the regulatory context has already gone one round before the United States Supreme Court.<sup>14</sup>

The responses on both sides of the debate were frequently emotive and defensive. Although an enormous amount of effort was invested by all the participants to the debate in identifying, analyzing, and debating the standards of conduct expected of lawyers, the extent and depth of the controversy suggested that the time had come for some comprehensive reflection on the evolving standards of lawyer responsibility in the regulatory context. Furthermore, the regulatory misadventures of accountants, seeming to parallel and, at times, even outdo those of lawyers,<sup>15</sup> indicated that there was good cause for lawyers to inform themselves about the manner in which the accounting profession had responded to similar problems. After all, lawyers and accountants had been jointly implicated by no less a figure than Judge Stanley Sporkin who, while writing in a case involving one of the most notorious of all the collapsed savings and loan

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12. See, e.g., Harris Weinstein, *Attorney Liability in the Savings and Loan Crisis*, 1993 U. ILL. L. REV. 53 (discussing issues of professional responsibility arising out of the savings and loan crisis and concluding that education about the governing rules of professional responsibility needs to be improved); Harris Weinstein, Chief Counsel, Office of Thrift Supervision, United States Department of the Treasury, Remarks before the Pennsylvania Association of Community Bankers (Mar. 23, 1992); Harris Weinstein, OTS Chief Counsel, Issues of Professional Responsibility Arising from the Savings and Loan Failures, Remarks delivered at the University of Michigan Law School (Mar. 24, 1992) [hereinafter *Michigan Speech*]; Harris Weinstein, OTS Chief Counsel, Remarks on Duties of Depository Institution Fiduciaries in 55 Banking Rep. (BNA) 510 (1990); Carolyn B. Lieberman & Neil J. McCarthy, *OTS Regulatory Actions Against Lawyers* (distributed at the annual meeting of the ABA in San Francisco (Aug. 10, 1992)).

13. Carolyn B. Lieberman & Dwight C. Smith, *Comments of the Office of Thrift Supervision on the Report and Recommendations of the ABA Working Group on Lawyers' Representation of Regulated Clients* (Aug. 1993).

14. *O'Melveny & Myers v. Federal Dep. Ins. Corp.*, 114 S. Ct. 2048 (1994) (holding that state law rather than federal common law applies in determination of whether knowledge about fraudulent conduct of S&L officers could be imputed to FDIC suing as a receiver).

15. The most recent of the many large settlements involving accounting firms is that by the firm of Deloitte & Touche, which agreed to pay \$312 million to settle all RTC, FDIC, and OTS claims against it. See, e.g., Barry Meier, *Deloitte & Touche Will Pay \$312 Million in S&L Cases*, N.Y. TIMES, Mar. 15, 1994, at C1 (nat'l ed.) (detailing the Deloitte & Touche settlement); *OTS Lists Deloitte's S&L Sins; 3rd Party Suit Adds a Few*, 2:24 BANK LAW. LIAB. 8, App. E (Apr. 1, 1994). Accounting firms have faced substantial liability in other jurisdictions as well. See, e.g., Joshua Mills, *Accounting Settlement in Australia*, N.Y. TIMES, Jan. 26, 1994, at C3 (nat'l ed.) (detailing the \$97 million settlement paid by KPMG Peat Marwick of Australia to settle claims by the State of Victoria with respect to the firm's audit in 1988 of the Tricontinental Group merchant bank, owned by the State Bank of Victoria, which collapsed in 1990). See also Ken McGuire, *Emergent Trends in Bank Supervision in the United Kingdom*, 56 MOD. L. REV. 669, 684-89 (1993) (discussing the role of accountant liability for the collapse of BCCI in England, and the resulting changes in the role of auditors).

associations, spoke in terms strongly suggesting that the two professions had substantially facilitated the improper transactions which led to the thrift's demise.<sup>16</sup>

In the face of such august censure, not even the stoutest defenders of either profession could plausibly attribute the long string of substantial settlements in the regulators' favor exclusively to governmental bullying and opportunism or isolated instances of professional wrongdoing. The legal profession, in particular, had been slow to acknowledge, and perhaps even to recognize, that serious questions had been raised regarding the adequacy of its codes of behavior and the actual levels of compliance these codes had been receiving.<sup>17</sup> The defensive posture of many lawyers, justified or not, has failed to reassure the public that the organized bar is able and willing to engage in self-criticism or to submit itself to external scrutiny.<sup>18</sup>

Perceiving the need for some calmer and broader professional introspec-

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16. *Lincoln Savings & Loan Ass'n v. Wall*, 743 F. Supp. 901 (D.D.C. 1990). In *Wall*, the court wrote:

Keating testified that he was so bent on doing the "right thing" that he surrounded himself with literally scores of accountants and lawyers to make sure all the transactions were legal.

The questions that must be asked are:

Where were these professionals, a number of whom are now asserting their rights under the Fifth Amendment, when these clearly improper transactions were being consummated?

Why didn't any of them speak up or disassociate themselves from the transactions?

Where also were the outside accountants and attorneys when these transactions were effectuated?

*Id.* at 919-20.

17. See Stanley Sporkin, *Lawyer and Accountant Responsibility*, Remarks before the Conference on Lawyers & Accountant Liability and Responsibility (Dec. 10, 1993), reprinted in REFORMING LEGAL ETHICS IN A REGULATED ENVIRONMENT 483-84 (1994) (suggesting that the accounting profession has been more constructively responsive to criticism than the legal profession).

See also IN THE PUBLIC INTEREST: A SPECIAL REPORT BY THE PUBLIC OVERSIGHT BOARD OF THE SEC PRACTICE SECTION, AICPA (Mar. 1993) (distributed to the delegates of the December meeting and detailing the accounting profession's responses to the criticisms arising from the S&L crisis); The Board of Directors of the American Institute of Certified Public Accountants, *Meeting the Financial and Reporting Needs of the Future: A Public Commitment from the Public Accounting Profession* (June 1993), reprinted in REFORMING LEGAL ETHICS IN A REGULATED ENVIRONMENT 525 (1994).

18. For an extensive critique in this vein, see Susan P. Koniak, *When Courts Refuse to Frame the Law and Others Frame It to Their Will*, 66 S. CAL. L. REV. 1075 (1993), reprinted in REFORMING LEGAL ETHICS IN A REGULATED ENVIRONMENT 439 (1994). See also Steve France, *Exoneration Through Denial*, THE RECORDER, Feb. 4, 1994, at 6 (asserting that the New York State Bar, which had concluded that there was no foundation for the OTS complaints against Peter Fishbein in the *Kaye, Scholer* case, provided an example of the legal profession's "defensive shadowboxing"). One media story even seemed to suggest collusion between lawyers and regulators to defraud the public. See Alison Frankel, *What Paul, Weiss Didn't Want You to Know*, AM. LAW., Dec. 1993, at 70 (suggesting that the settlement by the law firm in favor of the regulators in the sum of \$45 million served to avoid a much larger claim of \$300 million by the RTC).

One of the most reflective, challenging, and constructive diagnoses of the apparent unwillingness of the bar to address the ethical concerns arising out of the recent agency enforcement actions and lawsuits against lawyers is a forthcoming article by Ted Schneyer. Ted Schneyer, *From Self-*

tion, the Securities Law and Banking Law Committees of the Federal Bar Association decided to sponsor the American Law Institute-American Bar Association Conference on Lawyer and Accountant Liability and Responsibility. The invitational conference was held in Washington, D.C. on two bitterly cold days in December 1993. Perhaps the weather helped to cool passions; for whatever reason, the participants, including lawyers, accountants, present and former regulators, and journalists, produced a lively and mutually informative discussion. The issues reviewed in this Article reflect the concerns and thoughts that seemed most important to the participants. The materials that resulted from the conference provide a wide-ranging chronicle of the central themes that now inform the responsibilities, both legal and ethical, of lawyers, law firms and, to some extent, the accounting profession as well.

## I. POLICY STRATEGIES

### A. HOW SHOULD PROFESSIONAL CONDUCT BE EVALUATED?

From the lawyer's perspective, the evaluation and reform of lawyers' professional ethics and legal liability might be addressed from two familiar perspectives. First, there are certain modes of professional conduct that society considers to be "basic" or "fundamental." These include, for example, the need to observe certain standards of "professional" decorum or dignity even if alternative standards of conduct would not impair the effectiveness of the profession. Second, there is the concern for utility which addresses questions such as: what is the appropriate behavior for getting the job done effectively and efficiently?; and, is this behavior compatible with other utility concerns society might have? The two perspectives are of course connected. We think that lawyers should not undermine the court's dignity because the court might lose its authority in the eyes of those subject to its jurisdiction. On the other hand, it seems that "insiders," namely members of the profession and their immediate clients, tend to take some issues for granted, whereas outsiders tend to demand a clear utilitarian justification for any rule that favors the profession.

These two perspectives have been in evidence in the debate over the conduct and regulation of banking lawyers. Lawyers and their immediate clients place great value on principles of loyalty, confidentiality, and due process. Yet Rule 1.6 of the *Model Rules of Professional Conduct* (*Model Rules*),<sup>19</sup> which emphasizes the right of the client to the near total loyalty

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*Regulation to Bar Corporatism: What the S&L Crisis Means for the Regulation of Lawyers*, 35 S. TEX. L. REV. 201 (forthcoming 1994).

19. *Model Rule* 1.6 provides:

(a) A lawyer shall not reveal information relating to representation of a client unless

and confidentiality of the lawyer, can be difficult to defend when looked at from the instrumental perspective of the regulator who has a statutory responsibility to gain access to information only the client and the client's lawyer have. We can defend client confidentiality in instrumental terms, arguing that without it a client cannot receive the zealous representation we believe to be fundamental. We might argue, again in instrumental terms, that even where a client is committing wrong, it is better that the client be induced to seek the counsel of a good lawyer, who might dissuade the client from continuing the wrongdoing, in the knowledge that he or she will not be "betrayed," than that the client should withhold information from the lawyer. Worse still, the client might seek the services of a dishonest or incompetent lawyer. But when the argument in favor of client confidentiality is formulated in such utilitarian or instrumentalist terms, the very appeal to utility itself arouses many competing utilitarian arguments. For example, a regulator might argue that the potential harm a malefactor might wreak is so great that the value of zealous legal representation is outweighed by the need to protect public or other personal property.

However strongly lawyers might believe in the "fundamental" nature of lawyer/client confidentiality rules, public discourse and decisionmaking are overwhelmingly utilitarian. Hence, any defense of the traditional codes of professional responsibility against regulatory claims to increased public accountability had better be couched in utilitarian terms. But the same also applies to proponents of enhanced professional liability or higher professional standards of conduct. Merely insisting that lawyers and accountants should not provide "assistance" to wrongdoers won't do. This insistence just begs the question as to what lawyers and accountants *should* do when confronted by actual or potential client wrongdoing. Although the ultimate weighing process will inevitably be influenced by individual judgments as to what is most important, the question in utilitarian terms is: what norms would induce the patterns of behavior that most efficiently protect the client

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the client consents after consultation, except for disclosures that are impliedly authorized in order to carry out the representation, and except as stated in paragraph (b).

(b) A lawyer may reveal such information to the extent the lawyer reasonably believes necessary:

- (1) to prevent the client from committing a criminal act that the lawyer believes is likely to result in imminent death or substantial bodily harm; or
- (2) to establish a claim or defense on behalf of the lawyer in a controversy between the lawyer and the client, to establish a defense to a criminal charge or civil claim against the lawyer based upon conduct in which the client was involved, or to respond to allegations in any proceeding concerning the lawyer's representation of the client.

from overbearing government while, at the same time, not increasing the potential for wrongdoing, at least, and decreasing that potential, at best?

The second half of the query spurs the greatest differences of opinion. Private lawyers are inclined to acknowledge no more than that they should refrain from contributing to wrongdoing, the active prevention of wrongdoing being the responsibility of the regulators. The regulators, on the other hand, are burdened by too many responsibilities and strapped by too few resources. They are inclined to see lawyers and accountants as constituting well-placed sources of information and assistance. It would only be realistic to recognize that, to the extent that the legal profession cannot (and does not) claim absolute freedom from public responsibility, the regulators have a legitimate societal claim to some assistance from them. Again, the question is how much? The answer will often depend on a delicate judgment as to when and where some kind of "lawyer-gatekeeping" responsibility can be highly effective.

These concerns were raised on many occasions during the December meeting, though often in down-to-earth practical terms that tended to disguise the underlying issues just described. Some private practitioners, for example, made the familiar assertion that the costs of legal representation would rise because of the enhanced liability imposed on lawyers by enforcement actions, civil suits, and the extensive "due diligence" duties implicit in regulatory (and some judicial) demands that lawyers should independently determine the reliability of representations made by them on behalf of their clients. It was noted that many law firms' legal costs have already risen — either through delays, greater billings, or increased insurance premiums.

Such assertions seem hard to gainsay. After all, *someone* is going to have to cover these costs, but the fact that costs will rise does not prove that the regulators' position is wrong. It all depends on whether these costs are worth expending and whether they should be incurred. This assessment depends, in turn, upon (1) whether less expensive legal representation is sufficient to cover the societal responsibilities expected of depository and other regulated institutions as a condition for their operation, and (2) whether lawyers are more cost-efficient preventers of wrongdoing than are regulators.<sup>20</sup>

Perhaps the best analytical framework for evaluating the relative costs and benefits of stricter professional codes and enhanced liability is the one elegantly developed by Professor Reinier Kraakman.<sup>21</sup> Addressing the

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20. The term "cost" is used in its broadest sense to include the inevitable cost of invading client privacy.

21. Reinier H. Kraakman, *Corporate Liability Strategies and the Costs of Legal Controls*, 93 YALE L.J. 857 (1984) [hereinafter Kraakman, *Corporate Liability Strategies*]; Reinier H. Kraakman, *Gatekeepers: The Anatomy of a Third Party Enforcement Strategy*, 2 J.L. ECON. & ORG. 53 (1986)



problem of underenforcement, which is what generates demands for enhanced and broader liability for wrongdoing in many regulated industries including banking and securities, Professor Kraakman identifies three principal occasions in which underenforcement is likely to occur.<sup>22</sup> The first is that of "asset insufficiency," in which the recoverable assets of the harmed institution or the wrongdoer cannot compensate for the harm.<sup>23</sup> This would occur where the institution has suffered losses in the marketplace as a result of improper actions by management or its advisors, where the perpetrators of harm to the institution have insufficient recoverable assets, or where the institution has been "looted" and the wrongdoers either cannot be traced or have wasted or concealed their ill-gotten gains. Asset freeze orders and deep pocket lawsuits are strategies designed to compensate for "asset insufficiency" and, at least to this extent, are directly relevant to our own assessments of the proper balance between representative and client liability.

The second situation in which underenforcement occurs is that of "sanction insufficiency,"<sup>24</sup> where the scale of liability for sanctions is an insufficient incentive for lawful and safe action on the part of those who have the capacity to influence the institution. Congress clearly acted to improve "sanction sufficiency" when it passed the Financial Institutions Reform, Recovery and Enforcement Act of 1989,<sup>25</sup> thereby dramatically intensifying and broadening the scope of liability in the banking industry to administrative and criminal sanctions. Similarly, the battle in the courts, between the FDIC and RTC on the one hand and institution-affiliated parties (IAPs) on the other, over whether IAPs should be liable for "gross negligence" or "simple negligence,"<sup>26</sup> seems clearly based on agency efforts not only to increase recovery but also to broaden the scope of liability to all wrong-

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[hereinafter Kraakman, *Gatekeepers*]. For application of Professor Kraakman's views in the current context, see, e.g., Lawrence G. Baxter, *Fiduciary Issues in Federal Bank Regulation*, 56 LAW & CONTEMP. PROBS. 7, 36-37 (1993); Lawrence G. Baxter, *Judicial Responses to the Recent Enforcement Activities of the Federal Banking Regulators*, 59 FORDHAM. L. REV. 193, 237-38 (1991); George H. Brown, *Financial Institution Lawyers as Quasi-Public Enforcers*, 7 GEO. J. LEGAL ETHICS 637, 692 (1994); Howell E. Jackson, *Reflections on Kaye, Scholer: Enlisting Lawyers to Improve the Regulation of Financial Institutions*, 66 S. CAL. L. REV. 1019, 1021, 1049-61 (1993); David B. Wilkens, *Making Context Count: Regulating Lawyers After Kaye, Scholer*, 66 S. CAL. L. REV. 1145, 1161-65 (1993).

22. See Kraakman, *Corporate Liability Strategies*, *supra* note 21, at 867-88 (identifying asset insufficiency, sanction insufficiency, and enforcement insufficiency as likely to lead to underenforcement).

23. *Id.* at 868-76.

24. *Id.* at 876-88.

25. 12 U.S.C. § 1821 (1994).

26. See, e.g., *Resolution Trust Corp. v. Gallagher*, 10 F.3d 416 (7th Cir. 1993) (holding that FIRREA preempts federal common law and created cause of action solely for gross negligence in a suit by FDIC against thrift's former officers and directors); *Federal Dep. Ins. Corp. v. Harrington*, 844 F. Supp. 300 (N.D. Tex. 1994); *Federal Dep. Ins. Corp. v. Canfield*, 967 F.2d 443 (10th Cir. 1992), *cert. denied*, 113 S. Ct. 516 (1992) (holding that FIRREA does not preempt state statutory law

doers, no matter how slight their fault might be, thereby once again improving "sanction sufficiency."

In both the areas of asset and sanction sufficiency, Congress and the agencies have probably reached the outer limits of political feasibility. Yet this broadening and intensification of liability for wrongdoers still seems inadequate when considered from the regulators' point of view. The regulatory perception should not come as a surprise. Given their limited budgets, the amount of regulatory intrusion in which agencies can engage before an industry becomes smothered, and the inherent problem of regulatory lag (in which the necessary information reaches a regulator too late to prevent the harm), the agencies find themselves in the situation described by Professor Kraakman's third category, namely that of "enforcement insufficiency."<sup>27</sup> Enforcement insufficiency seems glaringly obvious in the context of securities and banking regulation, even if not elsewhere. The problem seems to lie at the very heart of the disputes between lawyers and regulators over their respective responsibilities in these two industries.

The most immediate remedy for enforcement insufficiency, when Congress will not or cannot provide the funding for more regulators and when regulators simply cannot get accurate and timely information, is to use "whistleblowers" and, more importantly for present purposes, "gatekeepers," from among the industry's own employees and outside professionals. Judge Sporkin's frustrated question — "where were the professionals?" — rests on an implicit assumption of third party responsibility. Lawyers and accountants, in the court's view, should have either refused to assist in the transactions that facilitated Keating and his companies' misdeeds or have reported them to the regulators. Many of the disputes over the role of lawyers and accountants stem from disagreement concerning the wisdom of this basic assumption.

Professor Kraakman again provides a number of helpful distinctions for evaluating the utility of these third party liability strategies.<sup>28</sup> First, whistleblowing, which involves direct disclosure of the wrongdoing to the regulators, should be distinguished from gatekeeping, which involves the direct responsibility of preventing or discouraging wrongdoing.<sup>29</sup> Whistleblowing, though already a limited feature of banking and securities regulation for employees and accountants, is much more controversial when applied to lawyers because it directly conflicts with the powerful confidentiality injunctions contained in ethical codes which apply some variant of *Model Rule 1.6*.

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or common law permitting actions against officers and directors of failed bank for simple negligence).

27. Kraakman, *Corporate Liability Strategies*, *supra* note 21, at 888-96.

28. Kraakman, *Gatekeepers*, *supra* note 21, at 61 *et seq.*

29. *Id.* at 58.

It would be helpful, when calls for increased lawyer responsibility are made, for proponents to be clear whether they would go so far as to impose whistleblowing responsibilities on lawyers. By doing so, the full extent to which traditional confidentiality rules are under challenge would be apparent and the relative efficiency of whistleblowing and confidential lawyering could be addressed.

Gatekeeping responsibilities, as distinct from whistleblowing, might take different forms, each more or less efficient in preventing wrongdoing, and each more or less controversial from the perspective of lawyers and their clients. As Professor Kraakman observes, lawyers and other professionals often have private market incentives to perform some type of gatekeeping function.<sup>30</sup> For example, lawyers pay a price if they acquire a reputation for having sleazy clients so they have an incentive to avoid serving such clients. On the other hand, there are often opposing incentives. For example, in a competitive environment, a lawyer might not be prepared to lose a bad client even if retaining that client would impair the lawyer's reputation. In the present context, the very existence of demands for greater professional responsibility indicates some level of market failure, with private incentives apparently being insufficient to induce an appropriate level of gatekeeping behavior. These demands suggest that there may be a need for "public" as opposed to "private" gatekeeping, in which some gatekeeping responsibility should be thrust upon the professionals, despite their inclinations, because public policy demands that this role should be played.<sup>31</sup> If lawyers won't act as gatekeepers out of their own inclinations, they could be forced to do so by means of strict norms and greater liability exposure.

A helpful distinction drawn by Professor Kraakman is between "bouncer" and "chaperone" gatekeepers.<sup>32</sup> Bouncer gatekeepers are expected to deny the would-be wrongdoer their services or endorsements altogether, while chaperone gatekeepers "detect and disrupt misconduct in an unfolding relationship with enforcement targets."<sup>33</sup> These two models provide strategic options that have differing implications for the bar, the application of its ethical codes, and the costs of legal representation. Under either model, the lawyer is not free to turn a blind eye to the real intentions of the client. But, under the chaperone model, the lawyer may not have to resign when a client persists in wrongdoing despite the lawyer's advice to the contrary, whereas under the bouncer model a lawyer should insist on lawful conduct by the client and resign if the client does not comply. Under the bouncer model, the lawyer would also be obliged to climb the corporate

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30. *Id.* at 60.

31. *Id.* at 62.

32. *Id.*

33. *Id.* at 63.

ladder where the wrongdoer is a subordinate within the organizational structure.

The contrasting approaches of the SEC and the OTS in the *Carter & Johnson*<sup>34</sup> and *Kaye, Scholer*<sup>35</sup> cases respectively provide good examples of two regulators assuming gatekeeper liability yet acting on differing conceptions of what gatekeeping should entail. In the *Carter & Johnson* case, the SEC concluded that *chaperone* gatekeeping appropriately captured the kind of gatekeeping responsibilities it had in mind after analyzing the long-term efficacy of this form of gatekeeping over its more severe counterpart. Reflecting on what a lawyer should do when faced with the wrongdoing of a subordinate within the client's corporate structure, the commission took the view that a direct approach to the corporation's board of directors was a possible, but not necessary, course of action.<sup>36</sup> What was important, in the commission's view, was "some prompt action that leads to the conclusion that the lawyer is engaged in efforts to correct the underlying problem."<sup>37</sup> The commission believed that "[t]he lawyer's continued interaction with his client will ordinarily hold the greatest promise of corrective action."<sup>38</sup>

The OTS, on the other hand, insisted in *Kaye, Scholer* and subsequent cases that a lawyer must climb the corporate ladder *whenever* the subordinate in the client institution refuses to comply with the law, failing which the lawyer will have no practical alternative but to resign.<sup>39</sup> This view expresses the *bouncer* conception of gatekeeping, reflecting a judgment by the agency that it is preferable that the lawyer should deny the institution all future assistance rather than continue to represent the institution in the knowledge that illegality is being perpetrated by its subordinates or has been left uncorrected.

Arguments over which role is best seem to turn on differing judgments as to which is really more effective, and even feasible, as a practical matter. The OTS position is perfectly rational and consistent with its determination

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34. See *In re Carter and Johnson*, [1981 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 82,847 (March 25, 1981) (stating that, so long as a lawyer is acting in good faith and exerting reasonable efforts to prevent violations of the law by the lawyer's client, the lawyer's professional obligations have been met).

35. *Kaye Scholer*, OTS AP-92-19 (1992).

36. *In re Carter and Johnson*, [1981 Transfer Binder] Fed. Sec. L. Rep. (CCH) at ¶ 84,172.

37. *Id.*

38. *Id.* at ¶ 84,173.

39. See *Kaye Scholer*, OTS AP-92-19, Notice of Charges ¶ 55, Consent Order ¶ 16. See generally *LABORERS IN DIFFERENT VINEYARDS?*, *supra* note 6, at 198-200, 203; *FINAL REPORT*, *supra* note 10 (commenting that OTS regulators had endorsed attorney resignation when efforts to prevent wrongdoing have proven unsuccessful). The OTS has recently softened its approach to the question of resignation, now asserting only that the attorney must "consider resignation." See Dwight C. Smith & Lewis A. Segall, *OTS Activity Addressing Lawyer Conduct reprinted in REFORMING LEGAL ETHICS IN A REGULATED ENVIRONMENT* 44, 46 (1994) (stating that if highest corporate authorities fail to correct unlawful conduct an attorney should consider resignation).

to ensure that the directors of depository institutions take an active role in the institution's management. But the SEC would reach a different judgment as to which gatekeeping role is more likely to prevent illegality. Most lawyers would prefer the SEC approach for the obvious reason that it leaves the decision in their hands, as the discretionary language of *Model Rule 1.13* would seem to have intended.<sup>40</sup>

It is doubtful whether arguments based purely on morality, doing "the right thing," will ever make a difference. Each side believes it holds the higher moral ground. Cases where attorneys have violated well accepted standards of conduct usually prove uncontroversial. However, where informed and significant portions of the bar have clashed with regulators over what the standards actually are, I have never met a lawyer who does not sincerely believe that he or she is being perfectly upright in taking a stand

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40. *Model Rule 1.13* provides:

- (a) A lawyer employed or retained by an organization represents the organization acting through its duly authorized constituents.
- (b) If a lawyer for an organization knows that an officer, employee or other person associated with the organization is engaged in action, intends to act or refuses to act in a matter related to the representation that is in violation of law which reasonably might be imputed to the organization, and is likely to result in substantial injury to the organization, the lawyer shall proceed as is reasonably necessary in the best interest of the organization. In determining how to proceed, the lawyer shall give due consideration to the seriousness of the violation and its consequences, the scope and nature of the lawyer's representation, the responsibility of the organization and the apparent motivation of the person involved, the policies of the organization concerning such matters and any other relevant considerations. Any measures taken shall be designed to minimize disruption of the organization and the risk of revealing information relating to the representation outside the organization. Such measures may include among others:
  - (1) asking for reconsideration of the matter;
  - (2) advising that a separate legal opinion on the matter be sought for presentation to appropriate authority in the organization; and
  - (3) referring the matter to higher authority in the organization, including, if warranted by seriousness of the matter, referral to the highest authority that can act in behalf of the organization as determined by applicable law.
- (c) If despite the lawyer's efforts in accordance with paragraph (b), the highest authority that can act on behalf of the organization insists upon action, or a refusal to act, that is clearly in violation of law and is likely to result in substantial injury to the organization, the lawyer shall resign in accordance with Rule 1.16.
- (d) In dealing with an organization's directors, officers, employees, members, shareholders or other constituents, a lawyer shall explain the identity of the client when it is apparent that the organization's interests are adverse to those of the constituents with whom the lawyer is dealing.
- (e) A lawyer representing an organization may also represent any of its directors, employees, members, shareholders or other constituents, subject to the provision of Rule 1.7. If the organization's consent to the dual representation is required by Rule 1.7, the consent shall be given by an appropriate official of the organization other than the individual who is to be represented, or by the shareholders.

against the regulators' interpretation. I doubt the club of moral righteousness will prove effective as a means of changing opinions or behavior.<sup>41</sup> The framework of analysis pioneered by Professor Kraakman helps us to focus on what is truly important in any debate concerning the role of the professions in preventing client wrongdoing, namely, the question of efficacy from all points of view. His concepts help us to ask difficult, but equally fair, questions about, for example, whether lawyers could provide more assistance to regulators by denying their services to industry miscreants, whether it is more efficient and cost effective to impose complicated internal committee structures on law firms in order to ensure that no inexperienced lawyer ever handles a depository institution client without supervision,<sup>42</sup> or whether we should have lawyers insure against the risk of client wrongdoing.

#### B. IS BANKING REGULATION A SPECIAL CASE?

The current uproar over professional conduct has arisen in the context of the S&L scandal. Is this problem peculiar to this area of practice?

From a social cost point of view, the fact that the depository institution clients of lawyers and accountants are insured by funds under federal agency custodianship and backed by the full faith and credit of the United States, in other words, the US taxpayer, surely introduces into the cost/benefit analysis an important factor that is normally not present in most other areas of legal practice. As Harris Weinstein has emphasized, "deposit insurance is a fact of life" that brings to the banking industry not only stability but also the moral hazard that counteracts the incentives for bankers to act responsibly.<sup>43</sup> The reduction in market discipline created by deposit insurance produces corresponding pressure on the regulators to provide other mechanisms for protecting the insured institutions from the harm their managers and owners can inflict upon them. In a world of scarce regulatory resources, a demand is generated for gatekeeper assistance.

The phenomenon of government-backed insurance and accompanying taxpayer exposure is not present in most other industries.<sup>44</sup> Hence, the

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41. There is obviously no accounting in this assessment for the views of the cynic who believes that lawyers only perceive that to be right which is in their immediate self-interest.

42. See, e.g., *In re Schilling and Jones, Day, Reavis & Pogue*, OTS No. AP 93-31 2-5 (Apr. 1993) (order to cease and desist imposing an internal committee structure on the law firm of Jones, Day, Reavis & Pogue).

43. Harris Weinstein, *Moral Hazard Deposit Insurance and Banking Regulation*, 77 CORNELL L. REV. 1099, 1100 (1992).

44. This is not to say that it does not exist in less obvious forms. For example, federal emergency assistance creates a moral hazard for the owners and developers of property that are exposed to natural dangers such as earthquakes and hurricanes. It could be argued that these owners, developers, and their professional service providers, should be required to observe greater

regulatory pressures on the professionals who service those industries is correspondingly less. But there are no clear dividing lines, particularly where other people's money is at risk. It has long been the case, for example, that lawyers engaged as experts in registered securities offerings and in preparing documentation on behalf of the client are required to perform a reasonable investigation to verify the facts supplied by the client (i.e., observe "due diligence"). The rationale underlying these requirements is that the public and buyers and sellers of securities are entitled to rely upon the representations involved with such transactions.<sup>45</sup> Tax lawyers are also expected to observe due diligence under certain circumstances.<sup>46</sup> Indeed, similar reasoning has been extended by state regulators in the insurance field, where it has been argued that lawyers representing insurance companies might owe gatekeeping duties of some kind to the regulators in addition to any duties they owe their clients.<sup>47</sup>

These examples suggest that the kinds of issues raised in the current debate are of relevance across a wide range of practice whenever there is some public risk at stake.<sup>48</sup> They might also provide some support for the view, expressed by many commentators who have been critical of the legal profession, that banking lawyers have merely been engaging in the same "greek chorus" in which their securities and tax law counterparts engaged during the late seventies and early eighties.

On the other hand, in weighing the costs and benefits of changed professional responsibilities, we should not leave out of the equation some unusual and significant cost and liability factors. While it is true that there is a strong similarity to the protests of the legal profession during the two eras, there are some very fundamental differences regarding the attitudes of the regulators concerned and the kinds of sanctions involved. Whereas the OTS has taken a severe, highly public approach to enforcement against lawyers

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safeguards than would be appropriate in the case of property in areas that are less likely to draw on federal assistance.

45. These duties derive from section 11 of the Securities Act of 1933, section 10(b) of the Securities Exchange Act of 1934 and its accompanying Rule 10b-5, and numerous other related securities law provisions. *See generally*, ROBERT J. HAFT, *LIABILITY OF ATTORNEYS AND ACCOUNTANTS FOR SECURITIES TRANSACTIONS* chs. 1-2 (1993-94), *reprinted in part in* REFORMING LEGAL ETHICS IN A REGULATED ENVIRONMENT 107 (1994) (discussing standards of liability employed by various courts under Rule 10b-5).

46. *See* 31 C.F.R. § 10.33 (1993) (promulgating rules governing attorneys who give tax shelter opinions).

47. *See, e.g.*, *LABORERS IN DIFFERENT VINEYARDS?*, *supra* note 6, at 290-94 (reviewing state insurance regulatory actions against insurance industry professionals).

48. Indeed, Judge Sporkin suggests that the debate is relevant even in the context of products liability, where " 'playing the rules' keeps a known dangerous substance or product in the market place for virtually unlimited periods of time." Stanley Sporkin, *The Need for Separate Codes of Professional Conduct for the Various Specialties*, 7 GEO. J. LEGAL ETHICS 149, 151 (1993), *reprinted in* REFORMING LEGAL ETHICS IN A REGULATED ENVIRONMENT 479 (1994) [hereinafter *Separate Codes*].

and accountants, the SEC seems to have taken a milder and more low-key approach in its own actions against the professions.<sup>49</sup> Furthermore, the sanctions that can be wielded by the SEC, even after the 1990 reforms, are quite moderate when compared with those available to, or at least asserted by, the OTS.<sup>50</sup> Since this difference between the actions and capabilities of the two regulators tends to be ignored by those who express impatience with the protests of lawyers, it is worth reminding ourselves of the ranges of sanctions that are available against professionals by the SEC, the federal banking agencies, and many other agencies.

## II. REMEDIES

### A. AGENCY SANCTIONS AGAINST LAWYERS

All agencies possess the power to impose *some* form of disciplinary sanction on the lawyers and accountants who represent clients before them.<sup>51</sup> As a general rule, any lawyer who is a member in good standing of the bar of the highest court of any state can represent a person before any federal government agency.<sup>52</sup> Some agencies also permit accountants to represent clients in agency proceedings.<sup>53</sup> While agencies cannot impose additional restrictions on the lawyer's initial right to appear before the agency without special statutory authority,<sup>54</sup> the power of any agency to impose *discipline* and even *disbarment* for attorney misconduct is regarded by the courts as a strongly implied, perhaps even an "inherent," aspect of

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49. The SEC acts against lawyers and accountants almost exclusively through its disciplinary Rule 2(e) procedures, and it issues *prospective* guidance for the professions instead of applying new standards in unprecedented cases. See *LABORERS IN DIFFERENT VINEYARDS?*, *supra* note 6.

50. See *LABORERS IN DIFFERENT VINEYARDS?*, *supra* note 6, at 272-75.

51. See generally Michael P. Cox, *Regulation of Attorneys Practicing Before Federal Agencies*, 34 CASE W. RES. L. REV. 173, 174 (1983-84) (discussing agency powers to regulate practice before them).

52. See 5 U.S.C. § 500(b) (1994) (providing that individuals who are members in good standing of the bar of the highest court of a state may represent person before United States administrative agencies upon the filing of a written declaration that he is qualified to do so). There is a special exception in the case of lawyers and agents representing clients before the Patent Office, which has special admission requirements. For example, the Patent Bar exception is contained in § 500(e). See also 35 U.S.C. §§ 31-33 (1994) (governing practice before the Patent Office).

53. See 5 U.S.C. § 500(c) (1994) (permitting accountants to practice before the Internal Revenue Service); accountants are treated as "practicing" before the SEC for disciplinary purposes when discharging their statutory responsibilities under the federal securities laws. See, e.g., *Davy v. Securities & Exchange Comm'n*, 792 F.2d 1418 (9th Cir. 1986) (affirming judgment by the SEC against an accountant who had engaged in improper professional conduct); *Touche Ross & Co. v. Securities & Exchange Comm'n*, 609 F.2d 570 (2d Cir. 1978) (affirming that the SEC may conduct an administrative proceeding to determine if accountants should be suspended from practicing before the commission).

54. See, e.g., *McDaniel v. Israel*, 534 F. Supp. 367 (W.D. Va. 1982) (invalidating an additional client-authorization requirement imposed by the Social Security Administration because it was not necessary for the efficient administration of the agency's program).



the agency's statutory mandate.<sup>55</sup> Many agencies therefore include, as part of their rules of procedure, rules providing for discipline in cases of lawyer misconduct. The SEC's Rule 2(e) is perhaps the most well known example,<sup>56</sup> but such rules are common to most agencies. Thus, when two attorneys practicing before the Interstate Commerce Commission were found to have surreptitiously represented both a client and the client's competitor and had successfully warded off both the resulting civil and state bar disciplinary actions, the agency was still able to reprimand and suspend them from practice before the agency.<sup>57</sup>

Some agencies, in particular the banking agencies and to a lesser extent the SEC, also possess much more severe implements of administrative discipline. In the banking agencies, attorneys, accountants, and other institution-affiliated parties can be hit with heavy civil money penalties,<sup>58</sup> ordered to make restitution for losses suffered by an Insured Depository Institution (IDI),<sup>59</sup> and/or permanently removed from any participation in the banking industry.<sup>60</sup> These sanctions, imposed through administrative, not judicial, proceedings,<sup>61</sup> have constituted the principal vehicle by which the OTS has imposed its expectations of lawyer and accountant conduct.<sup>62</sup>

A third sanction that might be wielded by an agency (through the judicial process) is rarely available; indeed, it is perhaps unique to the arena of

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55. See *Touche Ross & Co.*, 609 F.2d at 582 (holding that the SEC acted within its statutory authority when using Rule 2(e) to discipline professionals appearing before it).

56. 17 C.F.R. § 201.2(e) (1993); See also James R. Doty, *Regulatory Expectations Regarding the Conduct of Attorneys in the Enforcement of the Federal Securities Laws: Recent Developments and Lessons for the Future*, 48 BUS. LAW. 1543, 1544 n.6 (1993), reprinted in REFORMING LEGAL ETHICS IN A REGULATED ENVIRONMENT 85, 86 (1994) (discussing Rule 2(e)). For the analogous OTS provisions, see 12 C.F.R. § 513 (1993).

57. *Polydoroff v. Interstate Commerce Comm'n*, 773 F.2d 372 (D.C. Cir. 1985). See also *Kingsland v. Dorsey*, 338 U.S. 318 (1949), *reh'g denied*, 338 U.S. 939 (1950) (applying disciplinary rules in the patent context). But see *Jaskiewicz v. Mossinghoff*, 822 F.2d 1053 (Fed. Cir. 1987) (remanding for agency reconsideration of "too severe" a two-year suspension).

58. 12 U.S.C. § 1818(i)(2) (1994). These penalties are quite independent of the civil penalties that can be sought through the judicial process by the U.S. Department of Justice under 12 U.S.C. § 1833a and other provisions. For an example of a Justice Department complaint that effected a large settlement by a law firm, see *United States v. Warner & Stackpole*, D. Mass. Civ. Action No. 93-10924K (filed Apr. 27, 1993). See also *Lawyers Accused of Fraud*, WALL ST. J., Apr. 28, 1993, at B10 (discussing Warner & Stackpole's \$500,000 settlement).

59. 12 U.S.C. § 1818(b)(6)(A) (1994).

60. 12 U.S.C. § 1818(e) (1994). See also, HAFT, *supra* note 45, at § 8.01 (discussing the less extensive but still potent powers of the SEC); Ralph C. Ferrara, et al., *Hardball! The SEC's New Arsenal of Enforcement Weapons*, 47 BUS. LAW. 33 (1991).

61. Limited judicial review is available after the agency proceedings are concluded.

62. Almost all of the cases brought by the OTS against lawyers and accountants and their respective firms were brought under these statutory enforcement powers and not under the agency's disciplinary rules of practice. In many cases, the charges upon which the action was based were explicitly founded upon alleged violations of professional standards of conduct, and, at least to this extent, the enforcement action in question served as a form of sanction for alleged unethical, though not necessarily unlawful, lawyer misconduct.

banking regulation. This is the power by the FDIC and the RTC to file civil damages suits against professionals and the firms who represented IDIs before these institutions were placed in conservatorship or receivership.<sup>63</sup> This ability to file suits for damages, which distinguishes the FDIC and RTC from other federal agencies, stems from the unusual bankruptcy regime for banking institutions. Under this regime, these two agencies become the conservators and receivers of failing and failed banks and thrifts. Both agencies, in their receivership capacities, automatically acquire possession of the documentary communications between the institutions and their professional agents, accede to the rights of the institutions themselves,<sup>64</sup> and are thus able to sue as the institutions in receivership. Large numbers of such suits have been filed by the FDIC and the RTC against lawyers, accountants, and their firms, and the agencies have often secured very substantial settlements as a result of these suits. *O'Melveny & Myers v. Federal Deposit Insurance Corporation*<sup>65</sup> provides a notable current example of such proceedings.<sup>66</sup>

Views will obviously differ on why there has been so much controversy concerning the role of lawyers and accountants in the S&L scandal. Judge Sporkin and others believe that there has been an endemic lapse of professional standards among banking lawyers and accountants. Even if this perception is correct,<sup>67</sup> the unusual ability of the FDIC and the RTC to bring such suits, their willingness to do so, and the OTS' aggressive use of its vast and unprecedented enforcement powers are surely important factors serving to explain the high level of controversy regarding the ethics of lawyers and accountants in recent years.

#### B. AGENCY ENFORCEMENT ACTIONS AND CIVIL SUITS AS VEHICLES FOR DEVELOPING PROFESSIONAL STANDARDS?

The preceding review of the actions an agency can take to impose

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63. See LABORERS IN DIFFERENT VINEYARDS?, *supra* note 6, at Part III (reviewing civil suits filed by the FDIC and RTC).

64. See 12 U.S.C. § 1821(d)(2)(A)(1) (1994) (FDIC: providing that the corporation, as conservator or receiver, succeeds to all rights, titles, power and privileges of the insured depository institution); 12 U.S.C. § 1441a(b)(4)(A) (1994) (RTC: laying out provisions similar to those for the FDIC regarding rights and privileges of insured depository institutions).

65. 114 S. Ct. 2048 (1994).

66. As this Article was being prepared, the RTC filed one of its largest suits ever against the Phoenix law firm of Streich Lang, claiming \$400 million in damages for alleged negligent and unprofessional performance in the firm's work for Western Savings and Loan Association. Resolution Trust Corp. v. Streich Lang, P.A., No. CIV94-0357-PHX-EHC (D. Ariz. filed Feb. 16, 1994). See *R.T.C. Sues Law Firm*, N.Y. TIMES, Feb. 17, 1994, at D-19 (nat'l. ed.) (detailing RTC action); *\$400 Million Suit Against Streich Lang Sets a Record*, 2(22) BANK LAW. LIAB. 16 (Mar. 4, 1994).

67. For a categorical rejection of this premise, see Arthur W. Leibold, Jr., *The Higher Calling*, Speech before The Conference on Lawyer and Accountant Liability and Responsibility (Dec. 10-11, 1993), reprinted in REFORMING LEGAL ETHICS IN A REGULATED ENVIRONMENT 325, 333 (1994).

sanctions for unprofessional conduct addresses the firepower with, but not the baselines from, which the agencies can proceed. In an ideal world, allegations of unprofessional conduct could be measured against prior, clear standards of conduct known to the person accused of their breach.

Unfortunately, in the continuously evolving regulatory context, it is unrealistic to expect that the standards will always be clear. Not only must the standards cover a very wide variety of potential actions, but they are also difficult to formulate except in the context of a real-life situation — usually the event that triggers the allegation of a breach! It is therefore not unusual for agencies to develop their expectations of professional conduct through the medium of disciplinary rulings, lawsuits, and enforcement actions.

This mode of proceeding is tolerable as a necessity, but only to a point. Where the sanctions are extremely severe or where there is a divergence of understanding between the regulators and the professionals as to either the legitimacy or the meaning of the standards being imposed, the ad hoc development of agency standards, imposed on a respondent who either could not know them or had reasonably believed the agency to be wrong in its expectations, is likely to generate a sense of grievance and to promote a counterproductive, defensive posture by the profession. This is exactly what occurred in response to the OTS enforcement actions.<sup>68</sup>

In an effort to reconcile the opposing tugs of due process and agency practicality, the ABA Working Group exhorted the federal banking agencies to use notice-and-comment rulemaking procedures whenever possible for the purpose of formulating special standards of professional conduct.<sup>69</sup> The Working Group also advocated that the banking agencies should follow the SEC's example by using prospective rulings whenever an ad hoc enforcement action was found to be the necessary occasion for formulating new standards.<sup>70</sup> While the banking agencies have not indicated whether they will adopt such procedures,<sup>71</sup> the OTS has begun using a limited consultative approach in developing its "attorney letter," which would impose a range of strict representational and disclosure standards, based on

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68. See, e.g., Arthur W. Leibold, Jr., *Zealous Representation of Thrift Clients: Can It Exist?*, Presented before The Conference on Lawyer and Accountant Liability and Responsibility (Aug. 8, 1993) *reprinted in* REFORMING LEGAL ETHICS IN A REGULATED ENVIRONMENT 337 (1994) (discussing *Kaye Scholer's* failure to challenge OTS freeze order pursuant to 12 U.S.C. § 1818(c)(2)); Dennis J. Lehr, *Balancing the Fourth Branch: Dealing With the Focus on Attorney Conduct*, 57 BANKING REP. (BNA) 305, 308 (1991), *reprinted in* REFORMING LEGAL ETHICS IN A REGULATED ENVIRONMENT 319 (1994) (discussing law firm reactions to FDIC regulations).

69. LABORERS IN DIFFERENT VINEYARDS?, *supra* note 6, at 213-23.

70. *Id.* at 217-20.

71. See Lieberman & Smith, *supra* note 13, at 27-30 (preliminarily rejecting such procedures).

the agency's interpretations of the *Model Rules*, for lawyers who represent S&Ls.<sup>72</sup>

This emphasis on stating professional standards *in advance* of enforcement serves to highlight the importance of many of the general questions posed during the December meeting, including whether there should be uniform national standards, whether there should be specialized codes of conduct, whether the existing codes of conduct are simply out of date, and how specific a code of conduct can and should be.

### III. ADEQUACY OF THE CODES OF CONDUCT

#### A. SHOULD THERE BE UNIFORM NATIONAL STANDARDS?

The federal agencies have national missions. Although often working through regional offices, their empowering legislation seldom authorizes discrimination along regional lines. As a consequence, they are expected to act with reasonable consistency throughout the country. The professionals who represent the regulated clients often do so either on a national basis or across regions that do not necessarily coincide with state lines. A recurring problem, therefore, is whether state-based codes of conduct are appropriate to the representation of heavily regulated clients.<sup>73</sup>

In the wake of earlier controversies concerning the role of securities lawyers, this question was examined by the Committee on Governmental Processes of the Administrative Conference of the United States, a federal government administrative law policy-making agency with extensive governmental and private membership. The committee reviewed the disciplinary actions against lawyers by the SEC, Treasury Department, and the Interstate Commerce Commission and concluded that "any current problems arising from the discipline of attorneys by federal agencies are not of such a magnitude or so widespread as to require legislative action or a Conference recommendation for the adoption of uniform federal standards."<sup>74</sup> On many occasions during the recent debate over the actions of the OTS against lawyers and law firms, however, regulators have emphasized the need to be able to rely on national standards when specific state standards

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72. Smith & Segall, *supra* note 39, at 41. An early draft of the attorney letter is reprinted in REFORMING LEGAL ETHICS IN A REGULATED ENVIRONMENT 51 (1994).

73. See Cox, *supra* note 51, at 195-213 (advocating delegation by Congress to the Office of Government Ethics of the power to promulgate uniform standards of conduct for attorneys practicing before federal agencies). See also Stephen B. Burbank, *State Ethical Codes and Federal Practice: Emerging Conflicts and Suggestions for Reform*, 19 FORDHAM URBAN L.J. 969, 969 (1992) (suggesting that the time has come to think seriously of a national bar and uniform federal norms of professional conduct).

74. Report of the Committee on Governmental Processes of the Administrative Conference of the U.S., DISCIPLINE OF ATTORNEYS PRACTICING BEFORE GOVERNMENT AGENCIES, 1982 ACUS (vol. II) 488 (1982).

would frustrate the responsibilities of the agency.<sup>75</sup> The OTS has itself relied heavily on the *Model Rules* when determining whether attorneys have violated the agency's expectations of professional conduct.<sup>76</sup> Although now roundly rejected by the United States Supreme Court, a similar argument for uniformity by the FDIC had been influential in persuading the court of appeals in *O'Melveny* to create a federal common law of attorney conduct that had the effect of producing a rule of decision that seemed to conflict with the California standards otherwise applicable to the firm.<sup>77</sup>

The regulator's need for national uniformity and the practitioner's need for certainty as to which standard of conduct actually does apply provide arguments in favor of national, uniform standards, even if these are agency specific standards. On the other hand, federal standards of attorney conduct would represent a substantial departure from the traditional approach to lawyer discipline, for at least two reasons.

First, the states have long been regarded as bearing the primary responsibility for imposing standards of conduct for lawyers.<sup>78</sup> Federal agencies have long managed to live with this state-by-state approach notwithstanding the obvious inconvenience involved. Second, the bar is organized along state lines and its deliberative and disciplinary mechanisms are all state oriented. Elevating the power to create standards of attorney conduct to the federal level would *transfer* power from the profession to the regulators, unless the regulators were to recognize the primacy of the American Bar Association. So far, the regulators have shown no such inclination.

It is hard to imagine that the regulators could muster sufficient political support for so great an invasion of what lawyers perceive as their most exclusive province. Some state legislatures have already reacted against the "federalizing" efforts of the OTS.<sup>79</sup> It is possible that many more would do so were there to be a more coordinated attempt by the federal agencies to

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75. See, e.g., Paul Gonson & John W. Avery, *Practicing Securities Law: A Search for Uniformity of Professional Standards*, Presented at The Conference on Lawyer and Accountant Liability and Responsibility (Dec. 10-11, 1993) *reprinted in* REFORMING LEGAL ETHICS IN A REGULATED ENVIRONMENT 489 (1994) (stating that state disciplinary codes do not adequately address attorney conduct in the context of highly specialized practice). See also *LABORERS IN DIFFERENT VINEYARDS?*, *supra* note 6, at 144-45 (reporting the views of regulators who met with the ABA Working Group).

76. See, e.g., Weinstein, *Michigan Speech*, *supra* note 12, at 21 (discussing issues of professional responsibility arising out of the savings and loan crises).

77. *Federal Deposit Ins. Corp. v. O'Melveny & Meyers*, 969 F.2d 744, 751 (9th Cir. 1992), *rev'd sub nom.* 114 S. Ct. 2048 (1994). For a critical analysis of FDIC and RTC resort to "federal common law," see Arthur W. Leibold, Jr., *Federal Common Law: Part II*, Presented at the Conference on Lawyer and Accountant Liability and Responsibility (Dec. 10-11, 1993) *reprinted in* REFORMING LEGAL ETHICS IN A REGULATED ENVIRONMENT 349, 359 (1994).

78. See *infra* note 86 (citing cases supporting state's responsibility over standards of conduct for lawyers).

79. See John C. Deal, *State Legislative Responses to the Professional Liability Crisis*, Presented at Conference on Lawyer and Accountant Liability and Responsibility (Dec. 10-11, 1993), *reprinted*

upset the current model. Even if the lawyers who represent clients that are subject to heavy federal regulation could be persuaded that federal standards were in their own interest, it might be difficult to persuade the bar as a whole that the transfer of power symbolized by federal standards was worth the gains in certainty.<sup>80</sup>

#### B. SHOULD THERE BE SPECIALIZED CODES OF PROFESSIONAL CONDUCT?

The perception that decisive and forceful action should be taken against lawyers, and the unprecedented scale of settlements by lawyers and law firms in favor of the regulators and the receivers of the institutions for whom they performed services, raise the question whether the existing principles and processes of professional discipline are inadequate, either because they are not sufficiently sophisticated for regulatory practice or because they are too ambiguous. This postulate has been proposed by Judge Sporkin. His view is that the time has come for the development and application of separate codes of professional conduct to the various areas of lawyer specialization.<sup>81</sup> Others have suggested that agencies themselves should develop their own specialist codes, like the model of the Patent Bar<sup>82</sup> or the American Academy of Matrimonial Lawyers,<sup>83</sup> to cover those who practice before them.

The view that the currently available rules of professional conduct are inadequate or too unsophisticated is, however, somewhat gainsaid by those regulators most involved in the actions taken against lawyers as a result of S&L failures. They have insisted that the existing state codes of professional responsibility, together with the *Model Rules* (where state codes are inconsistent with each other or where they conflict with important national regulatory responsibilities) and any applicable agency regulations, provide a

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in REFORMING LEGAL ETHICS IN A REGULATED ENVIRONMENT 195, 195-206 (1994) (discussing Ohio and Louisiana's efforts to undercut FIRREA standard of care).

80. It is quite possible, of course, that the organized bar might be unable to prevent the development of federal standards on a piecemeal basis, either by the agencies, by the courts, by Congress, or by some combination of these bodies. This discussion merely speculates on the prospects for reform by the bar itself.

81. Sporkin, *Separate Codes*, *supra* note 48, at 152. See also NATIONAL COMMISSION ON FINANCIAL INSTITUTION REFORM, RECOVERY AND ENFORCEMENT, ORIGINS AND CAUSES OF THE S&L DEBACLE: A BLUEPRINT FOR REFORM (A REPORT TO THE PRESIDENT AND CONGRESS OF THE UNITED STATES) 14 (1993) (proposing that "[t]he legal and accounting professions should develop specialized rules of professional responsibility for attorneys and accountants representing institutions receiving federal insurance or guarantees"); Steve France, *Unhappy Pioneers: For S&L Lawyers, Liability Has Displaced Ethics*, 7 GEO. J. LEGAL ETHICS 725, 734 (1994), reprinted in REFORMING LEGAL ETHICS IN A REGULATED ENVIRONMENT 499 (1994) (suggesting that a new "common law of lawyering" is being applied to lawyers of different specialties).

82. This course of action was offered as a possible option at the December meeting by conference participant Paul Gonson.

83. Sporkin, *Separate Codes*, *supra* note 48, at 152.

sufficiently developed basis for maintaining professional integrity through disciplinary and enforcement action.<sup>84</sup>

The second possibility, that the present standards of conduct are too uncertain, is much more important because the relevant professional codes are themselves unclear as to when they apply in situations involving federal government agencies. For example, the comment to *Model Rule 8.5*, which provides a choice of law mechanism in cases where conflicting standards of two jurisdictions are potentially applicable, recognizes that “[a] lawyer may be potentially subject to more than one set of rules of professional conduct which impose different obligations.”<sup>85</sup> Yet, in an endeavor to subject the attorney to only one *actual* set of rules, *Model Rule 8.5(b)* merely provides that either the rule of the admitting jurisdiction in which the lawyer principally practices, or the rule of another jurisdiction where the particular conduct in question has its predominant effect, will be the one that applies. While the *Model Rule* does not address agencies specifically, it should be obvious that a federal agency’s perception of “predominant effect” will quite possibly differ from that of the state court and state bar councils where the lawyer is located or licensed, particularly when a transaction based on state law, but covered or underwritten by federal deposit insurance, is involved.

Nor do the agencies own rules really offer much assistance regarding the actual standards to be observed. The SEC’s Rule 2(e), for example, speaks of denying the privilege of practice before the agency to any person found “to be lacking in character or integrity or to have engaged in unethical or improper conduct.” The reader is required to look elsewhere — to state codes, the *Model Rules*, and agency decisions — in order to ascertain what might constitute “unethical or improper conduct.” In other words, the present agency rules depend for their meaning on standards external to the rules, yet it is not clear which external standards should be used.

The double uncertainty created by the choice of law problems and the vagueness of the agencies’ own rules acquires great significance when the Damocletian sword of sanctions hangs over an attorney’s conduct. The lure of separate, agency-specific codes of professional responsibility is therefore quite apparent. At the same time, however, a move to a regime of discrete codes, in a world in which most activities are subject to some kind of federal regulation, would entail a substantial revision of the traditional role of the states in maintaining bar discipline and setting standards for attorney conduct, a role that has always been regarded as reposing at the core of a state’s sovereign powers.<sup>86</sup> Such a move would also impose on agencies the

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84. See *LABORERS IN DIFFERENT VINEYARDS?*, *supra* note 6, at 144-45, 147-48.

85. *MODEL RULE* Rule 8.5 cmt. (Disciplinary Authority, Choice of Law).

86. See, e.g., *Hoover v. Ronwin*, 466 U.S. 558, 569 n.18 (1984) (noting that regulation of the bar is

responsibility to develop such codes through an unavoidably cumbersome and contentious rulemaking process.<sup>87</sup> The very viability of the enterprise itself, premised on the notion that clear standards of conduct can be stipulated in advance and in the abstract, a notion to which I shall return later, is doubtful. It is small wonder, then, that many regulators and private attorneys alike share little enthusiasm for the notion of specialist codes.

### C. ARE THE MODEL RULES SIMPLY OUT OF DATE?

Even if agency, or industry, specific codes of professional conduct are not desirable, it might be argued that the present *Model Rules* and many of their state counterparts are anachronistic, insofar as they fail to address the realities and needs of modern regulatory practice. In the author's view, the need for reform is evident in at least three important areas.

First, as has already been argued, *Model Rule* 8.5 is deficient in addressing the jurisdictional conflicts between agencies and states. The geographic conception upon which the *Model Rule* is based, assuming as it does that multi-jurisdictional practice will be either rare or dominated by an easily-identifiable leading jurisdiction, is unrealistic in a regulatory practice where one's client might be subject simultaneously to complex federal agency regulation and to the continuous operation of state-based principles of commercial law. Such is certainly the situation with federally insured depository institutions. The lawyer's work product is bound to be governed by substantial principles of both state and federal law, and there ought to be some reliable method by which one can determine whose standards of conduct, the state's or the agency's, should be observed.

The second area in which the *Model Rules* seem to be inadequate is in relation to whether the lawyer owes a duty of candor to an agency. Whether a lawyer must disclose information to an agency, irrespective of the client's

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a sovereign function of the state); *Bates v. State Bar of Arizona*, 433 U.S. 350, 361 (1977) (stating that "the regulation of the activities of the bar is at the core of the State's power to protect the public."); *Goldfarb v. Virginia State Bar*, 421 U.S. 773, 792 (1975) (stating that "[t]he interest of the States in regulating lawyers is especially great since lawyers are essential to the primary governmental function of administering justice, and have historically been 'officers of the courts.'").

87. An agency might assert that its code of professional conduct should be regarded as "procedural," and hence exempt from the Administrative Procedure Act's notice-and-comment rulemaking requirements. See 5 U.S.C. § 553(b)(A) (1988) (exempting "interpretative rules, general statements of policy, or rules of agency organization, procedure, or practice" from Administrative Procedure Act notice-and-comment rulemaking requirement). However, it is quite possible that the substantive impact on attorneys of such a code would be sufficient to induce a court to construe the code as "substantive," thereby triggering the rulemaking proceedings involving the opportunity for notice and comment.

At the same time, it is fair to note that the organized bar can hardly claim greater efficiency in its production and revision of ethical standards. The Byzantine processes of both the ABA and the ALI are at least as cumbersome as federal rulemaking proceedings.



wishes, will depend, in part, on whether the lawyer is governed by *Model Rule 3.3*, 3.9, or 4.1. Rule 3.3 of the *Model Rules*, which applies to agency adjudicative proceedings, requires candor toward a "tribunal" *irrespective* of any duty of client confidentiality.<sup>88</sup> *Model Rule 3.9* extends this unqualified duty of candor to situations in which a lawyer is representing a client before an administrative tribunal in a "nonadjudicative proceeding."<sup>89</sup>

On the other hand, *Model Rule 4.1* covers a situation in which the lawyer is representing a client in transactions with persons other than clients including, according to the comment to *Model Rule 3.9*, the government during negotiations or "other bilateral transaction[s] with a government agency." Rule 4.1(b) of the *Model Rules* requires disclosure by the lawyer of information to nonclients *only to the extent that such disclosure is not prohibited by Rule 1.6*. *Model Rule 4.1* is therefore qualified by the attorney's duty in *Model Rule 1.6* not to reveal confidential client information without authorization from the client.<sup>90</sup>

The polar opposites of formal agency adjudication and bilateral negotia-

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88. *Model Rule 3.3* states as follows:

- (a) A lawyer shall not knowingly:
  - (1) make a false statement of material fact or law to a tribunal;
  - (2) fail to disclose a material fact to a tribunal when disclosure is necessary to avoid assisting a criminal or fraudulent act by the client;
  - (3) fail to disclose to the tribunal legal authority in the controlling jurisdiction known to the lawyer to be directly adverse to the position of the client and not disclosed by opposing counsel; or
  - (4) offer evidence that the lawyer knows to be false. If a lawyer has offered material evidence and comes to know of its falsity, the lawyer shall take reasonable remedial measures.
- (b) The duties stated in paragraph (a) continue to the conclusion of the proceeding, and apply even if compliance requires disclosure of information otherwise protected by Rule 1.6.
- (c) A lawyer may refuse to offer evidence that the lawyer reasonably believes is false.
- (d) In an ex parte proceeding, a lawyer shall inform the tribunal of all material facts known to the lawyer which will enable the tribunal to make an informed decision, whether or not the facts are adverse.

MODEL RULES Rule 3.3.

89. *Model Rule 3.9* states as follows:

A lawyer representing a client before a legislative or administrative tribunal in a nonadjudicative proceeding shall disclose that the appearance is in a representative capacity and shall conform to the provisions of rule 3.3(a) through (c), 3.4(a) through (c) and 3.5.

MODEL RULES Rule 3.9.

90. See LABORERS IN DIFFERENT VINEYARDS?, *supra* note 6, at 161-69, for an analysis of the interaction of these *Model Rules* in the context of a bank examination. For more recent attempts to apply the *Model Rules* to bank examinations, see, e.g., Kevin T. Pagoda, *The Lawyer's Proper Role in the Examination of Financial Institutions: Defining the Duty to Disclose After Kaye, Scholer*, 34 SANTA CLARA L. REV. 135 (1993); Charles W. Wolfram, *Parts and Wholes: The Integrity of the Model Rules*, 6 GEO. J. LEGAL ETHICS 861, 898-900 (1993).

tion seem clear enough. However, the discharge of statutory responsibilities cannot fairly be characterized as falling into one or the other of these categories. When an agency official is discharging a statutory responsibility that involves reaching decisions that have the force of law, on the basis of facts and circumstances that are stipulated in the statutory authorization as decisional prerequisites, the interaction between the official and the regulated client is not one of coequal negotiating partners. This is true notwithstanding the fact that a good deal of argument and negotiation might take place during the process leading up to the official decision. The *agency official* has the power to make the final decision, even without the consent or acquiescence of the private party. Furthermore, unlike the situation of two coequal negotiating parties, the entire regulatory scheme is likely to be predicated on a degree of cooperation on the part of the professional players involved that is not present in the case of private negotiations. Not only are the regulators short of resources and time, but *the complexity of the regulatory system itself* requires a substantial input of expertise by the professionals representing their regulated clients. Just as legislatures cannot function without the expert assistance of private lobbyists, so too would many agencies become quite choked if they had to implement their regulatory missions without the continuous assistance of private professionals. Private parties can walk away from negotiations, regulators cannot. And regulators often have to trust the representations made to them.

These special features of regulatory decisionmaking are obvious where private parties seek some statutory benefit. They are also present in more complex interactions between regulators and clients where elements of negotiation are indeed present. The bank examination has been used as the primary example of such a situation: a government bank examiner might spend considerable time in dialogue with the officers of a depository institution and their lawyers before reaching a decision to impose an adverse classification on some of the institution's assets. This classification could have substantial, negative regulatory effects on the institution. It is made in discharge of a statutory responsibility to ensure that the safety of the institution is reliably assessed.

In determining the lawyer's disclosure responsibilities in the bank examination context, Rule 3.3 of the *Model Rules* is irrelevant because the bank examiner is not a "tribunal" within the meaning of that Rule. The only potentially applicable rules are *Model Rule 3.9*, where a duty of candor notwithstanding the client's wishes would apply, or *Model Rule 4.1*, where the client can control whether the disclosure is made. Despite the fact that the institution's officers and lawyers might appropriately try to influence the examiner to reach an asset classification favorable to the institution, and although the examiner is likely to welcome their help in understanding the character of the asset in question, this process can hardly be characterized

realistically as a “negotiation or other bilateral transaction” subject to *Model Rule 4.1*.

On the other hand, Rule 3.9 of the *Model Rules* is equally unhelpful. What is meant by a “nonadjudicative proceeding?” The ABA Standing Committee on Ethics and Professional Responsibility recently asserted that “[w]hile a regulatory examination does not fit precisely into the category ‘negotiation or other bilateral transaction,’ it is more clearly suggested by these terms than it is by the terms ‘rule-making or policy-making.’”<sup>91</sup> The Committee therefore concluded that *Model Rule 4.1* applied, and not *Model Rule 3.9*. To an administrative lawyer, this assertion is surely astounding. It disregards entirely the substance of the transaction between the examiner and the client and focuses exclusively upon its procedural form. The examiner could terminate the “negotiations” at any point and quite validly enter an asset classification that, subject to the highly unlikely possibility that it might be set aside on judicial review, would have the force of law. Indeed, to the administrative lawyer the transaction looks a lot more like the “policy-making” process that the comment to *Model Rule 3.9* indicates is that Rule’s concern, though such a classification would also be clumsy.

The truth is that the *Model Rules* are inept in their application to the administrative process. They are premised on the polar opposites of adversary agency adjudication and bilateral, consensual negotiation and are manifestly deficient in coping with the complicated and nuanced range of interactions in which any heavily regulated client must engage in while dealing with administrative agencies.

The third zone of deficiency goes to the heart of the matter, namely, the unrealistically restrictive nature of *Model Rule 1.6*. The Rule forbids disclosure of confidential client information, contrary to the wishes of the client, in all situations except where the lawyer reasonably believes such disclosure to be necessary to prevent a client from committing a criminal act that the lawyer believes is likely to result in imminent bodily death or substantial bodily harm or where the disclosure is necessary for the lawyer to defend against certain claims brought against the lawyer by the client.<sup>92</sup> The Commission on Evaluation of Professional Standards, which drafted the *Model Rules*, included a provision in its draft Rule 1.6 that would have permitted the lawyer to reveal client confidences in order to “rectify the consequences of a client’s criminal or fraudulent act in the furtherance of which the lawyer’s services have been used.” This portion of the draft was rejected by the ABA House of Delegates when the *Model Rules* were

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91. ABA Comm. on Ethics and Professional Responsibility, Formal Op. 93-375, *supra* note 11. See also MODEL RULES Rule 3.9 cmt. (using “rule-making or policy-making” to describe the agency activity to which the Rule applies).

92. See *supra* note 19 (providing text of *Model Rule 1.6*).

adopted in 1983. More recent efforts to broaden the scope of permissible disclosure under *Model Rule* 1.6 have been rejected by the House.<sup>93</sup>

The ABA's rigidity in insisting on a rule that prevents disclosure to regulators in circumstances where a client is perpetrating a fraud on the regulator seems hard to justify when such frauds in the savings and loan industry might well have cost the taxpaying public billions of dollars. Some states permit, or even require, disclosure in order to prevent fraud or the commission of certain crimes other than those recognized by *Model Rule* 1.6.<sup>94</sup> The drafters of the ALI Restatement considered an alternative provision that would permit disclosure to prevent fraud by a client.<sup>95</sup> This

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93. See ABA Comm. on Ethics and Professional Responsibility, Formal Op. 92-366 (1992) (describing the history of efforts to reform Rule 1.6). See generally Ted Schneyer, *Professionalism as Bar Politics: The Making of the Model Rules of Professional Conduct*, 14 L. & SOCIAL INQUIRY 677, 719-24 (1989). The standing committee itself had to reason to some lengths to conclude that a lawyer can disavow to third parties an opinion produced for a client who intends to use that opinion after having informed the lawyer that the information upon which the opinion had been given was false. See *id.* (Dissent of Elliot, Goyette & McFarlain) (criticizing the standing committee's conclusion that a lawyer faced with fraudulent client conduct may "nosily withdraw" from the representation under *Model Rule* 1.6). For a discussion on the ensuing debate concerning the scope of disclosure permitted by Rule 1.6, see Geoffrey C. Hazard, Jr., *Lawyers and Client Fraud: They Still Don't Get It*, 6 GEO. J. LEGAL ETHICS 701 (1993); and Margaret C. Love & Lawrence J. Fox, *Letter to Professor Hazard: Maybe Now He'll Get It*, 7 GEO. J. LEGAL ETHICS 145 (1993). For a spirited defense of Rule 1.6, see Lawrence J. Fox, *OTS vs. Kaye, Scholer: An Assault on the Citadel*, 48 BUS. LAW. 1521, 1525-33 (1993).

94. See, e.g., MICHIGAN RULES OF PROFESSIONAL CONDUCT Rule 1.6(c)(3) (1988) (stating: "A lawyer may reveal confidences and secrets to the extent reasonably necessary to rectify the consequences of a client's illegal or fraudulent act in the furtherance of which the lawyer's services have been used."); MINNESOTA RULES OF PROFESSIONAL CONDUCT Rule 1.6(b)(3)-(4) (1985) (providing that a lawyer may reveal "the intention of a client to commit a crime and the information necessary to prevent a crime" and "confidences and secrets necessary to rectify the consequences of a client's criminal or fraudulent act in the furtherance of which the lawyer's services were used . . ."); NEW JERSEY RULES OF PROFESSIONAL CONDUCT Rule 1.6(c)(1) (1984) (providing that: "A lawyer may reveal such information to the extent the lawyer reasonably believes necessary to rectify the consequences of a client's criminal, illegal or fraudulent act in the furtherance of which the lawyer's services had been used."); NEW YORK CODE OF PROFESSIONAL RESPONSIBILITY Code DR 4-101(C)(5) (1990) (stating: "A lawyer may reveal confidences or secrets to the extent implicit in withdrawing a written or oral opinion previously given by the lawyer and believed by the lawyer still to be relied upon by a third person where the lawyer has discovered that the opinion or representation was based on materially inaccurate information or is being used to further a crime or fraud.") See also, George W. Bermant & Simon M. Lorne, *The Noisy Withdrawal*, 2:6 BUS. LAW. TODAY 40, 57 (Jul./Aug. 1993) (noting that the large majority of states that have used the *Model Rules* as the basis for their rules have refused to follow the restrictive approach of Rule 1.6).

95. See Draft Restatement, alternative draft § 73(4)(b), reprinted in REFORMING LEGAL ETHICS IN A REGULATED ENVIRONMENT 312 (1994) (imposing upon a lawyer to prevent or rectify the breach of a fiduciary duty owed to a non-client by a client when the non-client is reasonably able to protect its rights and when the duty would not significantly impair the performance of the lawyers obligation to the client). This alternative provision was rejected by the ALI Council by a vote of 15-14. RESTATEMENT OF THE LAW GOVERNING LAWYERS § 73(b) note 1 (Tentative Draft No. 7, 1994) [hereinafter ALI TENTATIVE DRAFT]. For a critical analysis of the ALI project insofar as the issue of confidentiality is concerned, see Fred C. Zacharias, *Fact and Fiction in the Restatement of the Law*

author believes that lawyers should be permitted, under their applicable codes of professional conduct, to disclose to regulators client information that is within their knowledge or reasonable belief<sup>96</sup> in order to prevent their clients from misleading regulators in the exercise of their statutory responsibilities. As Professor Robert Haft observed at the December meeting, if lawyers do not amend the Rules the courts will do it for them.

A comprehensive review of the *Model Rules* might suggest other areas in which they are anachronistic or crude when applied to the regulatory situation.<sup>97</sup> The three examples identified seem to be the most important for the present.

#### D. HOW SPECIFIC CAN AND SHOULD CODES OF CONDUCT BE?

Another strategy in the search for greater certainty might be the adoption of codes of conduct that are more specific than those presently applicable. Some critics of lawyer conduct speak as though the norms that lawyers are alleged to have violated are clear cut. In fact, in many situations the closer one looks at the disputes involved, the more difficult the answers seem to become. As one of the participants in the Conference on Lawyer and Accountant Liability and Responsibility observed afterwards, some of the attacks on the legal profession's apparent recalcitrance in complying with appropriate standards of conduct "were both entertaining and elegantly stated but they seemed . . . to grapple with the easy questions rather than the hard ones."<sup>98</sup> The ABA Working Group, and the regulators who met with the Working Group, also agreed that decisions regarding appropriate lawyer conduct under the *Model Rules* always require a careful and detailed evaluation of the factual circumstances in which the conduct arises. Indeed, the Working Group found that it had to proceed in its discussions with the

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*Governing Lawyers; Should the Confidentiality Provisions Restate the Law?*, 6 GEO. J. LEGAL ETHICS 903 (1993).

96. I do not mean to imply that an attorney has a duty to investigate and ascertain information that might impeach the validity of every client representation to a regulator.

97. Other possible, and also controversial, examples might be *Model Rule* 1.7 (governing conflicts of interest) and *Model Rule* 1.13 (governing the responsibility of a lawyer to report misdeeds by subordinate officials or employees within the organization to superiors). See, e.g., LABORERS IN DIFFERENT VINEYARDS?, *supra* note 6, at 197-212 (discussing the possible interpretations of these Rules and the differences of opinion between OTS lawyers and the organized bar). See also Sporkin, *Separate Codes*, *supra* note 48, at 150-51, (suggesting the need for special conflicts rules where holding companies and their subsidiaries are subject to divergent regulatory requirements); Stephen Gillers, *Model Rule 1.13(c) Gives the Wrong Answer to the Question of Corporate Counsel Disclosure*, 1 GEO. J. LEGAL ETHICS 289, 289 (1987) (arguing that Rule 1.13 is structured in a way that prevents corporate counsel from taking effective action to prevent corporate wrongdoing).

98. Letter from Lawrence J. Latto to the author (Dec. 29, 1993).

regulators by using lengthy and complicated hypotheticals, and even then, clear agreement on the right answers did not always emerge.<sup>99</sup>

A graphic example of the fact-contingent nature of applied ethics was recently provided by the ABA Standing Committee on Ethics and Professional Responsibility's opinion on the role of a lawyer during a bank examination.<sup>100</sup> Addressing questions as to when and whether a lawyer should attend bank examination meetings with a client whom the lawyer knows to be lying to the examiner, the committee was at pains to eschew classificatory labels (such as whether the lawyer is an "advocate" or an "agent"), rightly emphasizing that wrongdoing on the part of the lawyer will depend, very precisely, upon "what the lawyer does or says." In matters of practical ethics, context is almost everything, and generalized, abstract norms provide little meaningful assistance in the complex regulatory situations that can often develop when one is representing a regulated client.

Would it help to have more specific codes of conduct? The *Model Rules* and the current drafts of the American Law Institute's Restatement of the Law Governing Lawyers<sup>101</sup> are sometimes laconic to the point of vacuity. *Model Rules* 3.9 and 8.5 are such examples.<sup>102</sup> Furthermore, Lawrence Latto pointed out during the December proceedings that the ALI draft Restatement contains awkwardnesses and some apparent contradictions. For example, the present draft section 192 states in the first subsection that "[a] lawyer may advise a client concerning the applicability of law to the client's intended conduct, so long as the lawyer does not go further and engage in activities described in Subsection (2)."<sup>103</sup> The second subsection then states that "[a] lawyer must not assist the client when doing so would incur liability on the part of the lawyer."<sup>104</sup> Yet, if an agency takes the view that a lawyer should not engage in "loophole lawyering," the lawyer is caught in a Catch-22 dilemma. If she advises the client that there are two possible interpretations of a law or regulation, one of which the agency rejects but which might well be upheld in the courts, she breaches subsection (2) by exposing herself to agency enforcement liability. If, on the other hand, she decides because of subsection (2) not to advise the client about the disputed interpretation, she is not effectively discharging responsibilities permitted under subsection (1). The drafters are, of course, aware of this problem,

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99. See LABORERS IN DIFFERENT VINEYARDS?, *supra* note 6, at Part IV.

100. ABA Comm. on Ethics and Professional Responsibility, Formal Op. 93-375 (1993).

101. See Lawrence J. Latto, The American Law Institute's Forthcoming Restatement of the Law Governing Lawyers, Presented at the Conference on Lawyer and Accountant Liability and Responsibility (Dec. 10-11, 1993) *reprinted in* REFORMING LEGAL ETHICS IN A REGULATED ENVIRONMENT 277, 282-306 (1994) (describing the expected liability provisions of the Restatement of the Law Governing Lawyers) [hereinafter *Restatement of the Law Governing Lawyers*].

102. See *supra* text accompanying notes 90-91.

103. *Restatement of the Law Governing Lawyers*, *supra* note 101, at 283.

104. *Id.*

and they have added a third subsection designed to permit the lawyer to test the applicability or validity of the law or regulation in good faith.<sup>105</sup> Nonetheless, the difficulty of resolving the problem is apparent from the complicated structure of the draft section.

It is perhaps conceivable that certainty might be enhanced through the use of more detailed rules, drafted with modern regulatory problems in mind. But it is unlikely, given the complicated nature of modern regulation, that a comprehensive body of rules could be devised without doing considerable violence to the notion that such rules should also be easily accessible and understood. It might be unrealistic to pin great hopes on the prospect of resolving issues of uncertainty through drafting skills.

#### E. SHOULD MORE USE BE MADE OF INTERNAL CONTROLS AND COLLECTIVE RESPONSIBILITY?

The prospect of more effective internal controls was explored at the December meeting. Examples from the accounting profession were instructive. Westbrook Murphy, an attorney familiar with the workings of the big accounting firms, described the systems of peer review by accounting firms, second partner reviews of non-standard opinions that are proposed by engagement teams, firm procedure manuals, and general oversight and quality-control review by the profession's Public Oversight Board.<sup>106</sup> Partly analogous controls have already been instituted in many large law firms, sometimes at the insistence of the regulators.<sup>107</sup>

Internal controls over professional misconduct are likely to be imposed by a firm where the firm will itself be held liable for breaches incurred by its members and employees. Professor Schneyer has developed a powerful argument in favor of this collective liability model as a method of promoting stricter observance of ethical conduct in modern law firms.<sup>108</sup> Although lawyers have been concerned that the OTS was unfairly holding law firms responsible for the conduct of individual lawyers,<sup>109</sup> there is much to be said

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105. See *id.* (providing that "[a] lawyer may assist a client in an open, good faith effort to determine the applicability or validity of a law or court order.")

106. See IN THE PUBLIC INTEREST, *supra* note 17, at App. B (describing the accounting profession's self-regulatory programs).

107. See, e.g., *In re Schilling and Jones, Day, Reavis & Pogue*, OTS No. AP-93-31 2-5 (Apr. 1993) (requiring the law firm to institute policies providing for supervision within the firm of the work of lawyers representing insured depository institutions by a "Financial Institutions Practice Committee" and by appointing an experienced practitioner to serve as a "Financial Institutions Supervising Partner").

108. See generally, Ted Schneyer, *Professional Discipline for Law Firms?*, 77 CORNELL L. REV. 1 (1991) (arguing that a system of law firm discipline should supplement individual discipline for lawyers). For a recent review of the judicial developments in this area, see ALI TENTATIVE DRAFT, *supra* note 95, at 121-26.

109. See, e.g., Keith R. Fisher, *Statutory Construction and the Kaye, Scholer Freeze Order*

in favor of a collective liability approach. From the regulators' viewpoint, they can deputize the policing of individual lawyer misconduct to the firm. To the firm itself, the collective liability approach promotes at least some degree of self-policing and locates decisions regarding professional propriety at a level that more accurately reflects the collective manner in which modern law firms operate.

A surprising degree of support for the concept of law firm responsibility is to be found in certain pronouncements of the organized bar. As Professor Schneyer observes, the supervisory responsibilities imposed by *Model Rule* 5.1 seem to contemplate some collective responsibility on the part of law firms in addition to that imposed on the supervising partners.<sup>110</sup> An ALI-ABA committee has unsuccessfully proposed a peer review system.<sup>111</sup> Perhaps most significantly, the New York City Bar Association, recognizing that ethical breaches are often a reflection of systemic problems within the firm itself, has recently gone so far as to recommend that the New York State disciplinary rules should be amended to provide for the discipline of law firms as well as individual lawyers.<sup>112</sup>

Internal review committees, policies, and procedures would help to ensure that maverick or inexperienced attorneys are prevented from violating professional standards, thereby not only protecting the client and the regulators from harm but also avoiding liability for the firm itself. Unfortunately, such devices are inevitably bureaucratic. They come at the price of delay and expense for the client. Lawyers are understandably skeptical. Ironically, as an attorney who has specialized in representing accounting firms attested at the December meeting, practice manuals can themselves help to generate malpractice suits where they have not been followed.<sup>113</sup>

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Presented at the Conference on Lawyer and Accountant Liability and Responsibility (Dec. 10-11, 1993), reprinted in REFORMING LEGAL ETHICS IN A REGULATED ENVIRONMENT 371, 386-91 (1994) (observing that statutory definition of institution affiliated parties in the Federal Deposit Insurance Act, 12 U.S.C. § 1818(c)(1) was intended to denote individuals). See also LABORERS IN DIFFERENT VINEYARDS, *supra* note 6, at 84-86.

110. See Schneyer, *supra* note 108 at 17 (observing that lawyers in large firms should adopt structural mechanisms which will ensure compliance with professional responsibility obligations).

111. ALI-ABA Comm. on Continuing Professional Educ., A MODEL PEER REVIEW SYSTEM (Discussion Draft Apr. 15, 1980). See also Schneyer, *supra* note 108, at 40-41 (discussing peer review proposals and the arguments against their adoption).

112. See *Discipline of Law Firms*, *supra* note 8, at 250 (arguing that the promulgation of standards applicable to law firms will help firms minimize exposure to legal liability for conduct which could have been avoided).

113. The example cited was *Escott v. BarChris Construction Corp.*, 283 F. Supp. 643 (S.D.N.Y. 1968) (finding that an accounting firm had violated acceptable professional standards because of noncompliance with internal auditing program which conformed to generally accepted auditing standards). See also *Henricksen v. Henricksen*, 640 F.2d 880, 884-85 (7th Cir. 1981) (holding that the failure by stockbroker to follow its own noncompliance rules indicates an absence of reasonable diligence).



## F. DOES IT HELP TO MODIFY THE STANDARDS OF CULPABILITY?

The escalation of enforcement and malpractice suits against lawyers and accountants led many participants at the December meeting to speculate on the causes and efficacy of the current standards of culpability. Could a broader or more liberal standard of liability — “simple negligence” instead of “gross negligence”<sup>114</sup> — provide a more effective incentive for attorneys and accountants to avoid conduct that facilitates client wrongdoing? On the other hand, would this prove unfair to professionals?

Opinion seems deeply divided between those who believe that liability and enforcement suits against professionals are primarily designed to secure recovery from well insured defendants (deep pocket suits) and those who believe that there has been a general decline in professional standards.<sup>115</sup> Proponents of a lower culpability standard insist that lawyers have a duty to practice what Harris Weinstein has called “whole law,” in terms of which a lawyer “counseling a client in a gray area without clear guidelines . . . must advise banking fiduciaries that their conduct must be consistent with their fiduciary duties, and must meet their obligation to operate their institution safely and soundly.”<sup>116</sup> The implication is that wrongdoing on the part of client managers will be prevented by lawyer gatekeepers who point out to their clients the danger of their ways.<sup>117</sup>

Advocates of enhanced lawyer liability could indeed point to a growing trend within the legal profession as support for their position. Some law firms invite responsibility for the business mistakes of their clients when they hold themselves out as comprehensive advisers and business strategists. In particular, law firms who employ business consultants — in some cases, even as partners — for the specific purpose of broadening their appeal to clients can hardly be heard to complain when they are held responsible for the business judgments they influence.

Lawyers respond that, in areas involving highly discretionary judgments, lawsuits based on low culpability standards are palpably unfair and, to the extent that professionals are not prescient and are dependent on their

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114. See *supra* note 23 (discussing cases employing gross negligence standards of liability under FIRREA for attorney misconduct).

115. Compare, for example, the views expressed by Judge Sporkin, *supra* note 17 with Arthur Leibold, Jr., *The Higher Calling*, *supra* note 68 (debating the merit of specialized attorney codes of conduct).

116. See, e.g., Weinstein, *Michigan Speech*, *supra* note 12, at 11-12.

117. A similar strategy seems partly to underlie the attempt by regulators at the OTS to develop a theory of fiduciary duty that would extend the obligations lawyers have to their clients directly to the regulators as well. For a vigorous rejection of this theory, see, for example, Keith R. Fisher, *Nibbling on the Chancellor's Toesies: A "Roguish" Concurrence With Professor Baxter*, 56:1 LAW & CONTEMP. PROBS. 45 (1993), reprinted in REFORMING LEGAL ETHICS IN A REGULATED ENVIRONMENT 413 (1994).

client's own business judgments,<sup>118</sup> which sometimes turn out to be wrong, ineffective as a means of influencing professional behavior. Even worse, if this is correct, then liability would become arbitrary and not worth risking.

The difficulty is that one is dealing with "negligent," not intentional, action in an area involving *discretionary* judgments that are traditionally thought to be the preserve of management itself, not outside lawyers. As the commentary to *Model Rule 1.13* notes, "[w]hen constituents of the organization make decisions for it, the decisions ordinarily must be accepted by the lawyer even if their utility or prudence is doubtful. Decisions concerning policy and operations, including ones entailing serious risk, are not as such in the lawyer's province."<sup>119</sup> While it is also true that the lawyer must take action to prevent the organization from being injured by illegal activity,<sup>120</sup> holding a lawyer liable for business judgments that turn out to be wrong will have the effect of transferring principal responsibility for those judgments to lawyers. Whether encouraged by the actions of progressive law firms or not, the thought that the world of business might yet be further encumbered by the lawyer's methods is hardly uplifting.

Whichever view is correct, one result seems inevitable: broader liability would certainly create an incentive for firms to formalize their procedures more thoroughly in order to create a record of the care they have taken so that they can ward off future lawsuits. The unavoidable drift toward formality might be a price worth paying for enhanced gatekeeping by lawyers and accountants, but it is also a certain cost.

#### G. CAN WE EXPECT "HIGHER STANDARDS" FROM GOVERNMENT LAWYERS TOO?

One issue that received little attention during the controversy over the role of lawyers and accountants in the S&L scandal was the conduct of government lawyers themselves. Regulators have insisted that they are entitled to expect high standards of conduct by lawyers and accountants when these professionals perform services on behalf of clients that enjoy the benefit of public backing such as federally guaranteed deposit insurance. One would have thought that it goes without saying that the government lawyers should observe the highest standards themselves.<sup>121</sup> Yet, the view is

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118. See, e.g., *Resolution Trust Corp. v. Acton*, 844 F. Supp. 307 (N.D. Tex. 1994) (applying the Texas business judgment rule as a defense to negligence suits against the former directors and officers of failed financial institutions); *Federal Dep. Ins. Corp. v. Brown*, 812 F. Supp. 722 (S.D. Tex. 1992).

119. MODEL RULES Rule 1.13 cmt.

120. *Id.*

121. Federal agency lawyers are, of course, committed to the Federal Bar Association's *Model Rules of Professional Conduct for Federal Lawyers* (1990), but the effectiveness of these Rules, like the *ABA Model Rules*, is potentially a matter of dispute.

sometimes expressed that private lawyers should not complain when government lawyers “played hardball,” since this was the standard private lawyers set for themselves.

Views might differ over whether government lawyers should be expected to act in the long-term general interests of the public and not merely for short term adversarial advantage.<sup>122</sup> But, as a commentator observed at the December meeting, government lawyers themselves sometimes have been found to have engaged in unacceptable conduct in recent enforcement cases involving depository institutions.<sup>123</sup> Some judges have also chastised the conduct of counsel for the FDIC and RTC in malpractice suits brought on behalf of those agencies.<sup>124</sup> The issue has since moved to the fore as part of the Whitewater scandal, in which the FDIC has been accused of failing to observe conflict-of-interest rules in its use of law firms that had been previously engaged in representing the potential targets of the agency’s enforcement and malpractice actions.<sup>125</sup>

The political and competitive pressures that can lead to misconduct by government lawyers are surely real, even though government lawyers are often heard to deny that they allow themselves to be influenced by such factors. In formulating views as to whether uniform and/or specialized codes of professional conduct are needed, it is important to address the need both for provisions governing the appropriate conduct of government

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122. For an excellent scholarly review of this subject, see Catherine J. Lanctot, *The Duty of Zealous Advocacy and the Ethics of the Federal Government Lawyer: The Three Hardest Questions*, 64 S. CAL. L. REV. 951 (1991).

123. The cases cited at the meeting were *Kronholm v. Federal Dep. Ins. Corp.*, 915 F.2d 1171, 1173-74 n.1 (8th Cir. 1990) (where the court stated that it had been “left with the distinct impression that the government ha[d] attempted to mislead the court into applying [a] statute prior to its amendment under the apparent belief that it could affect the outcome of the case”); and *Bullion v. Federal Dep. Ins. Corp.*, 881 F.2d 1368, 1377 (5th Cir. 1989) (where the court found that the government lawyers had clearly engaged in an abuse of the discovery process that might have been “appropriate grounds for some form of sanctions” in another forum).

124. See, e.g., *Washington Bancorp. v. Said*, 812 F. Supp. 1256 (imposing Rule 11 sanctions against agency counsel for filing unripe claims); *Resolution Trust Corp. v. Nat’l Union Fire Ins. Co.*, No. 4:92CV727 ELF(CDP) (E. Mo. June 18, 1993) (described in 2:9 BANK LAW. LIAB. 10) (Aug. 6, 1993) (addressing a recommendation by magistrate that suit be dismissed as a sanction for discovery abuses by agency counsel). But see *Resolution Trust Corp. v. Bright*, 6 F.3d 336 (1993) (reversing a lower court’s disbarment and disqualification of an agency counsel).

125. See, e.g., *Senate GOP Attacks FDIC’s Findings on Madison-Rose, Seeks Review by FDIC*, 62 BANKING REP. (BNA) 384 (1994) (discussing a FDIC Report which found no conflicts of interest when the Rose Law Firm litigated an accountant malpractice case on behalf of the FDIC while representing Madison Guaranty before Arkansas securities regulators); Stephen Labaton, *Rose Law Firm, Arkansas Power, Slips as It Steps Onto a Bigger Stage*, N.Y. TIMES, Feb. 26, 1994 (late ed.) at 9. For the agency responses, see Federal Deposit Insurance Corporation, *Legal Division Report on the Retention of the Rose Law Firm for the Madison Guarantee Savings and Loan Conservatorship* (Feb. 17, 1994), reprinted in 2(22) BANK LAW. LIAB. at A1, D1 (Mar. 4, 1994); and Resolution Trust Corporation, *Memorandum to Jose Cappel: Rose Law Firm* (Feb. 6, 1994), reprinted in 2(22) BANK LAW. LIAB. at A1, D1 (Mar. 4, 1994).

lawyers and for effective mechanisms for disciplining such lawyers when these standards are violated.

H. ARE LAWYERS ENTERING TERRITORY ALREADY WELL TRODDEN BY ACCOUNTANTS?

Some commentators have suggested that S&L lawyers have entered a new realm of lawyering, one in which traditional standards have lost their application.<sup>126</sup> If this assessment is correct, it may be that the change in the role of lawyers is following the pattern set for the accounting profession during the course of this century.

The primary responsibility of accountants shifted from protecting the assets of the owner-employer from pilferage by employees to protecting the investing public from deception by fraudulent businesses. In the process, the concept of an independent accountant emerged as an essential feature of modern securities law, and accountants developed the all-important notion of *independence from their clients*. This path of evolution is certainly suggested by enforcement actions and judicial decisions imposing due diligence responsibilities on lawyers. Whereas it has long been accepted that the responsibilities of lawyers and accountants were fundamentally different,<sup>127</sup> it may be that this difference is disappearing.

The convergence of the respective scopes of lawyer and accountant responsibility will involve some far more fundamental changes than might be appreciated by the proponents of such convergence. For as long as we believe that individuals and organizations are entitled to zealous, loyal, and confidential legal representation, as distinct from external evaluation, it is hard to understand how a lawyer can be expected to provide that service while also performing an external policing function on behalf of the public or the regulators. One might be able to reconcile chaperone, and sometimes even bouncer, gatekeeping functions with the rest of a lawyer's responsibilities, but the cost of each of these additional duties has to be weighed against the loss to citizens of advice and representation that is *independent from the government*. As always, the hardest task is to strike a balance appropriate to a free society and a dynamic, evolving system of regulation.<sup>128</sup>

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126. See, e.g., Sporkin, *Separate Codes*, *supra* note 48; France, *supra* note 81.

127. See, e.g., *United States v. Arthur Young & Co.*, 465 U.S. 805, 817-18 (1984) (holding that there is no work product immunity for tax accrual work papers prepared by an accountant); *Rudolph v. Arthur Andersen & Co.*, 800 F.2d 1040, 1043-44 (11th Cir. 1986), *cert. denied*, 480 U.S. 946 (1987) (stating that accountants have a duty to disclose misstatements in financial statements because investors are likely to rely upon an accountant's work). See, e.g., HAFT, *supra* note 45, at § 6.01 (stating that: "The respective roles of attorneys and accountants in securities offerings are quite distinct.").

128. Compare A.A. Sommer, Jr., *Legislation Affecting the Liability of Accountants*, *reprinted in* REFORMING LEGAL ETHICS IN A REGULATED ENVIRONMENT 533 (1994) with Dan L. Goldwasser,

#### IV. CONCLUDING THOUGHTS

There seems to be a case for revising at least some of the rules governing the conduct and liability of attorneys who represent clients that are subject to statutory and regulatory duties. How much reform is unclear. Perhaps a major reform of the traditional standards of professional conduct is unnecessary. A number of commentators will disagree.

The task of overhauling, modernizing, or even merely modifying the present standards is likely to be a continuous process. Some issues, however, ought to be addressed immediately, particularly in the fields of banking and securities law: the severity of the administrative sanctions and the scope of potential malpractice liability in both fields of practice is so great that unless we work now to clarify and update the ground rules, lawyers will continue to be exposed to uncertain consequences for their actions. A refusal to respond will not insulate lawyers from liability: as more than one commentator at the December meeting emphasized, the regulators and the courts will act if lawyers don't. *Kaye, Scholer, O'Melveny & Myers*, and many similar cases already prove this proposition.